MISSISSIPPI LAW JOURNAL

THE NATURE AND DEVELOPMENT OF THE OIL AND GAS LEASE

Earl A. Brown

PROCEDURAL REFORM IN MISSISSIPPI—PART I

L. G. Fant, Jr.

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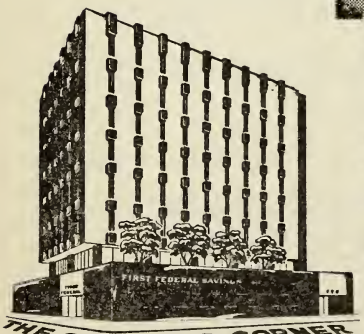

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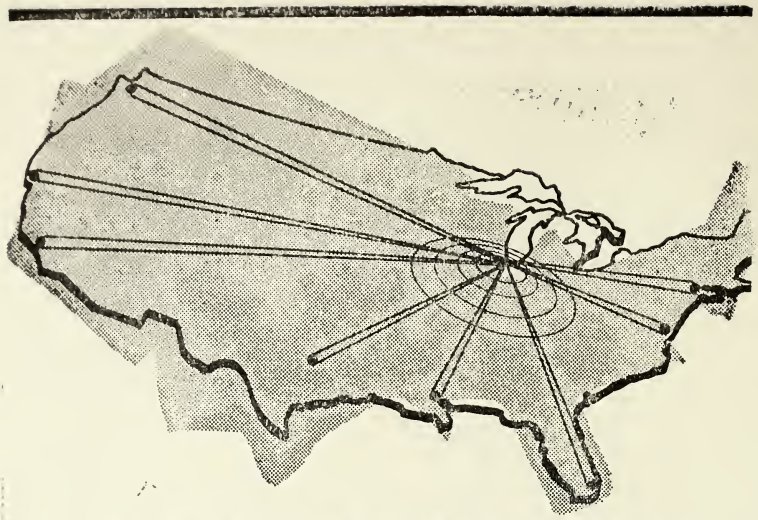

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THE NATURE AND DEVELOPMENT OF THE OIL AND GAS LEASE

*Earl A. Brown**

I. Introduction

The oil and gas lease was unknown to the common law, and for that reason it has been in a continuous state of evolution and development ever since the first lease was executed. As one distinguished oil and gas lawyer, Roy W. Johns, has said, "Oil and gas law has been in the same fluid state as the subject matter with which it deals."[1]

The first oil and gas lease was executed one hundred nine years ago, on July 4, 1853, five years before the first oil well was drilled. It consisted of eighty-nine words and reads as follows.

> Agreed this 4th day of July, A.D., 1853 with J. D. Angier of Cherrytree Township, in the county of Venargo, Pennsylvania, that he shall repair up and keep in order the old oil spring on land in said Cherrytree Township, or dig and make new springs, and the expense to be deducted out of the proceeds of the oil and the balance, if any, to be equally divided, the one-half to J. D. Angier and the other half to Brewer, Watson & Co., for the full term of five years from this date. If profitable.
>
> (Signed) Brewer, Watson & Co.
> (Signed) J. D. Angier[2]

The first producing oil well drilled in America, completed in 1859, was the Drake well, located at Titusville, Pennsylvania. The "lease" under which it was drilled contained some of the fundamentals of the modern lease, that is, the right "to bore, dig, mine, search for and obtain oil, salt water, coal and all materials existing in and upon said lands, and take and remove and sell the same . . ." It also specified a term—fifteen years, with the privilege of "renewal" for the same term. Also, it contained a provision for a royalty, called a "rental" in the lease, of "one-eighth of all oil as collected from the springs in barrels" furnished by the lessees.[3]

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*Attorney at Law, Dallas, Texas.

[1] ABA, Section of Mineral Law (1940).

[2] Southwestern Legal Foundation, Second Annual Institute on Oil and Gas Law and Taxation 6 (1951) [hereinafter cited as Foundation].

[3] *Id.* at 7.

Another interesting provision of that lease was the one that gave the lessee the right to purchase the royalty oil at "45 cents per gallon." Since there are 42 gallons in a barrel, that means the price of oil under that lease was $18.90 per barrel, as compared with a top price of $3.00 per barrel today. However, before the well was completed it evidently occurred to the lessee that the price was a little too steep, and by amendment to the lease the price was reduced to 12 cents a gallon or $5.04 per barrel, which is still an unusually good price, as judged by today's standards. Also, by amendment to the lease, the privilege of renewal of the fifteen year term was enlarged from fifteen to twenty-five years.

Another provision of the lease, which has a modern ring, required diligent operations, fixing a time for commencing operations, and termination for failure to comply with certain specified requirements.

Thus, most of the fundamentals of the modern oil and gas lease are found in that old lease executed in 1857—a granting clause, a term clause, royalty provisions, and requirements for operational diligence. The oil and gas leases of today represent principally a development and enlargement of the provisions of that early lease executed in 1857.[4]

II. The Modern Oil and Gas Lease

Due to limitations of time in presenting this paper, the development, step by step, of the modern oil and gas lease is omitted, and we come now to a consideration of modern oil and gas lease forms. First, let it be said that the courts do not recognize any "standardized" lease form.[5] There are estimated to be more than two hundred different oil and gas lease forms in use today in various parts of the oil producing areas. Therefore, each instrument must be interpreted in the light of its own peculiar provisions.

The estate created by an oil and gas lease has been variously stated by the courts of different jurisdictions to be real estate, an estate in land, an interest in land, a license to explore, an incorporeal hereditament, a chattel real, a profit a prendre, as well as other characterizations. And yet the name "lease," which is universally applied to this contract, is a misnomer. Such an instrument bears little resemblance to the kind of contract that creates a tenancy and the relation of landlord and tenant. It resembles a *lease* only in that it contains a term (but usually not a definite one) for which it shall remain in force, and provides for payments at regular intervals. These payments, however, are not for occupation of the surface of the land, as in the

[4]For an excellent historical discussion of the oil and gas lease by Leslie Moses see FOUNDATION 1-42.

[5]See, *e.g.*, Kansas Natural Gas Co. v. Board of Comm'rs., 75 Kan. 335, 89 Pac. 750 (1907). See generally FOUNDATION 1-42.

typical real estate lease, but are commutation payments for delay in drilling on the premises. Nevertheless, the term "lease" will undoubtedly continue to be used, regardless of its inherent significance and legal effect.

A. The Interest Transferred

1. *The Ownership in Place Theory*

Generally speaking, there are two theories of ownership in the oil and gas rights which a lessee acquires under an oil and gas lease today. Under the first doctrine it was said in a landmark case[6] that "gas and oil in place are minerals and realty, subject to ownership, severance and sale, while embedded in the sands or rocks beneath the earth's surface." Thus, in this theory of ownership, an oil and gas lease contains all the elements of a conveyance of real estate.

This doctrine represents the rule in Texas[7] and, with some individual variations based on the granting words, it is generally regarded as the law in Pennsylvania,[8] New Mexico,[9] North Dakota,[10] Michigan,[11] and Montana.[12] Mississippi is also an "ownership in place" state. An oil and gas lease here is considered as a conveyance of real estate,[13] and "the lessee's estate is a determinable fee in the minerals."[14]

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[6]Stephens County v. Mid-Kansas Oil & Gas Co., 113 Tex. 160, 254 S.W. 290 (1923), 29 A.L.R. 566 (1924).

[7]See, *e.g.*, Texas Co. v. Daugherty, 107 Tex. 226, 176 S.W. 717 (1915). See generally Walker, *The Nature of the Property Interests Created by an Oil and Gas Lease in Texas,* 7 TEXAS L. REV. 1 (1928).

[8]See, *e.g.*, Barnsdall v. Bradford Gas Co., 225 Pa. 338, 74 Atl. 207 (1909), 26 L.R.A. (n.s.) 614 (1910). See generally Comment, 4 U. PITT. L. REV. 274 (1938).

[9]See *e.g.*, Heath v. Gray, 58 N.M. 665, 274 P.2d 620 (1954).

[10]See, *e.g.*, Alfson v. Anderson, 78 N.W.2d 693 (N.D. 1956). These decisions consistently refer to an oil and gas lease as vesting in the lessee "an interest in real estate," but it should be remembered that an incorporeal hereditament has been called an "interest in real estate."

[11]See Jaenicke v. Davidson, 290 Mich. 298, 287 N.W. 472 (1939), where it is said that a lease of oil and gas constitutes an "interest" or "rights" in real estates and not an "option."

[12]See, *e.g.*, Stokes v. Tutvet, 134 Mont. 250, 328 P.2d 1096 (1958).

[13]See, *e.g.*, Calcote v. Texas Pac. Coal & Oil Co., 157 F.2d 216 (5th Cir.), *cert. denied,* 329 U. S. 782 (1946), 167 A.L.R. 413 (1947); Merrill Eng'r. Co. v. Capital Nat'l Bank, 192 Miss. 378, 5 So. 2d 666 (1942); Lloyd's Estate v. Mullen Tractor & Equip. Co., 192 Miss. 62, 4 So. 2d 282 (1941); Stokely v. State *ex rel.* Knox, 149 Miss. 435, 115 So. 563 (1928).

[14]Frost v. Gulf Oil Corp., 238 Miss. 775, 119 So. 2d 759 (1960); Koenig v. Calcote, 199 Miss. 435, 25 So. 2d 763 (1946). See generally Hall, *The Application of the Determinable Fee Theory in Construing the Mississippi Mineral Lease,* 19 MISS. L. J. 291 (1948).

2. *The Incorporeal Hereditament Theory*

Probably there is no clearer statement of this doctrine than is found in a landmark Oklahoma case,[15] where the court said that an oil and gas lease does not vest in the lessee "title to the oil and gas in said land and is not a grant of any estate therein, but is simply a grant of the right to prospect for oil and gas, no title vesting until such substances are reduced to possession by extracting same from the earth—an incorporeal hereditament."

This is the rule also in Kansas,[16] Indiana,[17] New York,[18] Illinois,[19] Arkansas,[20] Kentucky,[21] Wyoming,[22] Tennessee,[23] Washington,[24] Ohio,[25] California,[26] and West Virginia.[27]

B. Rules of Construction

Notwithstanding the two different theories of ownership mentioned above, there is little practical difference between them as to the results obtained in recovering oil and gas by the usual production methods. The law of capture appears equally applicable whatever the basic nature of the lessee's ownership. A concise statement of the rule of capture, by an authoritative writer, is as follows: "The owner of a tract of land acquires title to the oil and gas which he produces from wells drilled thereon, though it may be proved that part of such oil or gas migrated from adjoining lands."[28]

The fact that a lease conveys title to the oil "in place" does not

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[15]Kolachny v. Galbreath, 26 Okla. 772, 110 Pac. 902 (1910), 38 L.R.A. (n.s.) 45 (1911). This principle has been consistently followed in Oklahoma. See State v. Shamblin, 185 Okla. 126, 90 P.2d 1053 (1939), where the court said that in that state it had been "repeatedly and consistently held that such oil and gas mining leases are chattels real and therefore personal property."

[16]See, *e.g.*, Denver Nat'l Bank v. State Comm'n, 176 Kan 617, 272 P.2d 1070 (1954), *affirmance upheld on rehearing*, 177 Kan. 274, 279 P.2d 257 (1955).

[17]See, *e.g.*, Halbert v. Hendrix, 121 Ind. App. 43, 95 N.E.2d 221 (1950).

[18]See, *e.g.*, Wagner v. Mallory, 169 N.Y. 501, 62 N.E. 584 (1902).

[19]See, *e.g.*, Pickens v. Adams, 7 Ill. 2d 283, 131 N.E.2d 38 (1956).

[20]See, *e.g.*, Davis v. Collins, 219 Ark. 948, 245 S.W.2d 571 (1952).

[21]See, *e.g.*, Van Camp v. Evans, 306 Ky. 59, 206 S.W.2d 38 (1947), 173 A.L.R. 1256 (1948).

[22]See Boatman v. Andre, 44 Wyo. 352, 12 P.2d 370 (1932).

[23]See Morris v. Messer, 156 Tenn. 54, 299 S.W. 782 (1927).

[24]See Walla Walla Oil, Gas & Pipe Line Co. v. Vallentine, 103 Wash. 359, 174 Pac. 980 (1918).

[25]See, *e.g.*, Bach v. Ohio Fuel Gas Co., 160 Ohio St. 81, 113 N.E.2d 865 (1953).

[26]See, *e.g.*, Basin Oil Co. v. Baash-Ross Tool Co., 125 Cal. App. 2d 578, 271 P.2d 122 (Dist. Ct. App. 1954).

[27]See Charter v. Maxwell, 132 W. Va. 282, 52 S.E.2d 753 (1949).

[28]Hardwicke, *The Rule of Capture and Its Implications as Applied to Oil and Gas*, 13 TEXAS L. REV. 391, 393 (1935).

prevent the lessee from acquiring title to the oil or gas migrating into the reservoir under his leased land subsequent to the date of his lease, nor of losing title to the oil or gas draining from under his land into that portion of the reservoir underlying adjoining lands.[29] Likewise, a similar construction has been given the rule in the courts of the "incorporeal hereditament" states.[30]

Notwithstanding the fact that a majority of the states adhere to the view that an oil and gas lease is an "incorporeal hereditament" or a "chattel real," partaking of the nature of personal property, many of those states have found it necessary to apply to oil and gas leases legal principles and statutes intended for application to conveyances of real estate. For example, it is generally held that oil and gas leases and assignments thereof are instruments subject to recordation under the statutes relating to real estate.[31] Louisiana appears to be the only exception.[32] Also, oil and gas leases are at least "interests" in real property, and as such are within the statute of frauds.[33] A possible exception to this rule comes from the state of Washington.[34] And it is generally held that oil and gas leases should be executed and acknowledged with the same formalities as are required in conveyances of land, whether the lease be a chattel real, incorporeal hereditament or conveyance of real estate.[35]

It may be stated with assurance that the incidents of real estate ownership apply generally to oil and gas leases in the "ownership in place" states.[36] However, in the states which follow the non-ownership in place theory, there are instances where the laws with reference to real estate apply to oil and gas leases, and others in which they do not. Where the land leased is the homestead, it seems generally to be re-

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[29]See, *e.g.*, Brown v. Humble Oil & Ref. Co., 126 Tex. 296, 83 S.W.2d 935 (1935), 99 A.L.R. 1107.

[30]See, *e.g.*, Higgins Oil & Fuel Co. v. Guaranty Oil Co., 145 La. 233, 82 So. 206 (1919), 5 A.L.R. 411 (1920); Gruger v. Phillips Petroleum Co., 192 Okla. 259, 135 P.2d 485 (1943).

[31]See, *e.g.*, Callahan v. Martin, 3 Cal. 2d 110, 43 P.2d 788 (1935), 101 A.L.R. 871 (1936); Davis v. Lewis, 187 Okla. 91, 100 P.2d 994 (1940).

[32]See Arnold v. Sun Oil Co., 218 La. 50, 48 So. 2d 369 (1950).

[33]See, *e.g.*, Harris v. Tucker, 147 Okla. 210, 296 Pac. 397 (1931); Woodworth v. Franklin, 85 Okla. 27, 204 Pac. 452 (1921), 27 A.L.R. 590 (1923).

[34]See Walla Walla Oil, Gas & Pipe Line Co. v. Vallentine, 103 Wash. 359, 174 Pac. 980 (1918).

[35]See, *e.g.*, Beckett-Iseman Oil Co. v. Backer, 165 Ky. 818, 178 S.W. 1084 (1915); Kennedy v. Burns, 84 W. Va. 701, 101 S.E. 156 (1919). See generally 58 C.J.S. *Mines and Minerals* § 196 (1948).

[36]See, *e.g.*, Barnsdall v. Bradford Gas Co., 225 Pa. 338, 74 Atl. 207 (1909), 26 L.R.A. (n.s.) 614 (1910); Garza v. Del Montalavo, 147 Tex. 527, 217 S.W.2d 988 (1949). See generally 1A SUMMERS, OIL AND GAS §§ 155, 165 (perm. ed. 1954).

quired that the lease must be executed by both husband and wife.[37] And a mortgage on an oil and gas lease must be recorded in the records of real estate mortgages.[38] And it has been held that the right of recovery for breach of warranty in an assignment of an oil and gas lease is derived from the statute applying to breach of covenants for title in conveyances of real property.[39] On the other hand it was held in an early Oklahoma case, and followed by the supreme court since, that an oil and gas lease, being a "chattel real," is not within the requirements of a statute providing for a guardian's sale of real estate.[40] A qualification of this rule is announced in a West Virginia case.[41] In another Oklahoma case it was held that the filing of a judgment in the judgment record of a county, which by statute creates a lien on the judgment debtor's realty in that county, did not constitute a lien on an oil and gas lease owned by the debtor for the reason that an oil and gas lease is not real estate.[42]

In the matter of taxation, however, the decisions in the non-ownership states (except California) appear to be fairly uniform in holding that oil and gas leases do not constitute real estate within the meaning of the ad valorem tax statutes applicable to real estate.[43] In the "ownership in place" states there seems to have been no question about taxing an oil and gas lease or oil in the ground as realty.[44]

Finally, a federal court has refused to consider an oil and gas lease as exempt from the federal documentary stamp tax, applicable to instruments whereby any lands, tenements or other "realty" are sold and conveyed, even though the state court has held that an oil and gas lease is a "chattel real" and therefore personalty.[45]

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[37]See, *e.g.*, Sperry Oil & Gas Co. v. Chisholm, 264 U. S. 488 (1924); Carter Oil Co. v. Popp, 70 Okla. 232, 174 Pac. 747 (1918). See generally 40 C.J.S. *Homesteads* § 130(d) (1944).

[38]See Continental Supply Co. v. Marshall, 152 F.2d 300 (10th Cir.), *cert. denied*, 327 U.S. 803 (1945).

[39]Nicholson Corp. v. Ferguson, 114 Okla. 16, 243 Pac. 195 (1926).

[40]Duff v. Keaton, 33 Okla. 92, 124 Pac. 291 (1912).

[41]Ford v. Ball, 76 W. Va. 663, 86 S.E. 562 (1915).

[42]First Nat'l Bank v. Dunlap, 122 Okla. 288, 254 Pac. 729 (1927), 52 A.L.R. 126 (1928).

[43]See, *e.g.*, Ventura County v. Moynier, 207 Cal. 189, 277 Pac. 333 (1929); *In re* Hazelwood Oil Co., 195 App. Div. 23, 185 N.Y. Supp. 809 (1920), where oil and gas leases are made taxable by a special statute; State v. Shamblin, 185 Okla. 126, 90 P.2d 1053 (1939).

[44]See, *e.g.*, Stephens County v. Mid-Kansas Oil & Gas Co., 113 Tex. 160, 254 S.W. 290 (1923), 29 A.L.R. 566 (1924). Indeed the matter of extending tax statutes governing real estate to oil and gas leases in Texas may have been related to establishing the "ownership in place" rule in Texas, as the earlier decisions seemed to incline toward the non-ownership theory. In Emery v. League, 31 Tex. Civ. App. 474, 72 S.W. 603 (1903), the court characterized oil leases as "not conveyances of title but are in the nature of options."

[45]Phillips Petroleum Co. v. Jones, 176 F.2d 737 (10th Cir. 1949).

1. *General Rules of Construction of Oil and Gas Leases*

The general rule, announced in many cases and jurisdictions, is that if an oil and gas lease is susceptible of more than one interpretation or construction, it shall be construed most strongly against the lessee and in favor of the lessor.[46] This rule is exactly the opposite of the rule applied to leases generally, where it has been said that it is a "cardinal rule of construction that any doubt, uncertainty or ambiguity in a lease is to be construed most strongly against the lessor and in favor of the lessee."[47]

In the earlier cases the reason given by the courts for holding that a lease should be most strictly construed against lessee was because the lease was prepared by the lessee.[48] In later years, however, when the terms of an oil and gas lease are so often dictated by the lessor, or the parties use a printed form of lease not prepared by either of them, the rule of construction that the lease is to be most strongly construed against the lessee and in favor of the lessor is usually announced, without any qualifying words.[49]

There are occasions where one rule of construction may change the application of another such rule. In the late Texas case of *Gex v. Texas Company*[50] the instrument construed provided that the grantors *"do hereby grant, bargain, sell and convey* unto The Texas Company all of the oil, gas and other minerals" in a described tract of land. The instrument provided that the grantor should receive a royalty of one-eighth of the oil and gas produced from the land, the lessee to have the right to free use of oil and gas for operations conducted on the premises, the right to erect all necessary structures on the premises, and contained other provisions usually found in oil and gas leases. The issue was whether the instrument was a deed or an oil and gas lease. Texas is an "ownership in place" state, and the court held that the instrument was a "deed" to the minerals. It further held that the applicable rule of construction was the one that says a "deed" will be construed most

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[46]See, *e.g.*, Bodcaw Oil Co. v. Atlantic Ref. Co., 217 Ark. 50, 228 S.W.2d 626 (1950); Kies v. Williams, 190 Ky. 596, 228 S.W. 40 (1921); Frost v. Gulf Oil Corp., 238 Miss. 775, 119 So. 2d 759 (1960); Newman Bros. Drilling Co. v. Stanolind Oil & Gas Co., 157 Tex. 489, 305 S.W.2d 169 (1957).

[47]*In re* Mount Holly Paper Co., 110 F.2d 220 (3d Cir. 1940). See also 455 Seventh Ave. v. Frederick Hussey Realty Co., 295 N.Y. 166, 65 N.E.2d 761 (1946); City Hotel Co. v. Aumont Hotel Co., 107 S.W.2d 1094 (Tex. Civ. App. 1937); 51 C.J.S. *Landlord and Tenant* § 232(e) (1947).

[48]*E.g.*, Habermel v. Mong, 31 F.2d 822 (6th Cir. 1929), 67 A.L.R. 216 (1930); Bettman v. Harness, 42 W. Va. 433, 26 S.E. 271 (1896), 36 L.R.A. 566 (1897).

[49]See, *e.g.*, Frost v. Gulf Oil Corp., 238 Miss. 775, 119 So. 2d 759 (1960); Newman Bros. Drilling Co. v. Stanolind Oil & Gas Co., 296 S.W.2d 567 (Tex. Civ. App. 1956), *aff'd*, 157 Tex. 489, 305 S.W.2d 169 (1957).

[50]337 S.W.2d 820 (Tex. Civ. App. 1960).

strongly against the grantor and in favor of the grantee, and applied that rule in construing a royalty provision.

The Supreme Court of Oklahoma, in the case of *Eggleston v. Sinclair Oil & Gas Company*,[51] construed a similar instrument, that is, the grant was a perpetuity, the granting words were those usually found in a deed, there were royalty provisions in favor of the grantor, and other provisions usually found in an oil and gas lease. Oklahoma is an "incorporeal hereditament" state and the court held that the instrument was not a deed but an oil and gas lease, thus making applicable the rule that it should be construed most strongly in favor of the grantor (lessor) and against the grantee (lessee).

The doctrine of implying covenants in a contract is not new. It was a recognized principle of law before the courts began to construe oil and gas leases. However, the basis for implying covenants in an oil and gas lease is completely different from that which governs such implications in other contracts. The basis of this rule in contracts, other than oil, gas and mineral leases, is that the implied covenant exists only when it is necessary to imply certain duties and obligations in order to effect the purposes of the parties as expressed in the contract made.[52]

In another Texas case the Supreme Court said:

> It is not enough to say that an implied covenant is necessary in order to make the contract fair, or that without such a covenant it would be improvident or unwise, or that the contract would operate unjustly. *It must arise from the presumed intention of the parties as gathered from the instrument as a whole.*[53] (Emphasis added.)

And a standard authority basing its statement upon many reported cases, says: "An implied covenant is one inferred or implied in law from the words used and is based upon the presumed intention of the parties. Such covenants are not favored."[54]

Nevertheless, as applied to oil and gas leases, the covenants implied, as we shall see later, are independent of and in addition to the "words used" and "the intention of the parties" and "they are favored" in the construction of oil and gas leases in the "interest of promoting development." As said in a leading authority, "This covenant is to be implied from the relation of the parties and the object of the lease."[55] This case is often cited in support of the proposition that implied

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[51]132 Okla. 81, 269 Pac. 306 (1928).

[52]See, *e.g.*, Freeport Sulphur Co. v. American Sulphur Royalty Co., 117 Tex. 439, 6 S.W.2d 1039 (1928), 60 A.L.R. 890 (1929).

[53]Danciger Oil & Ref. Co. v. Powell, 137 Tex. 484, 490, 154 S.W.2d 632, 635 (1941), 137 A.L.R. 408 (1942).

[54]21 C.J.S. *Covenants* § 9 (1940).

[55]Sauder v. Mid-Continent Petroleum Corp., 292 U.S. 272 (1934), 93 A.L.R. 454.

covenants in oil and gas leases arise by operation of law and not by reason of the words used or the expressed intention of the contract.

However, there is a wide difference of opinion as to whether implied covenants in an oil and gas lease are implied in fact or in law. Professor A. W. Walker of the University of Texas reaches the conclusion that "the implication is viewed as one of fact and not of law."[56] Professor Maurice Merrill of the University of Oklahoma, a prolific writer who believes in more and broader implied covenants, thinks the implication is one of law, because as he very candidly states, "There is no basis upon which we can infer that lessors and lessees have in mind the implied covenant obligations when they contract."[57] It may be said, however, that the courts have experienced little difficulty in applying and enforcing these covenants regardless of whether their basis is in law or in fact.

2. *The Habendum Clause*

Some of the early oil and gas leases provided for terms that were perpetual;[58] some were to "continue in force until annulled by mutual agreement";[59] others provided for continuation of the lease and if "oil is found the right to pump to continue as long as rent is paid."[60] Then there were other leases that fixed the periods of duration for a long term of years with no "thereafter" clause.[61]

The next development was to add to the long definite or primary term a "thereafter" clause, which would extend the definite term for as long thereafter as oil or gas was produced. The final step was to make the long primary term shorter, usually from five to ten years. So, the clause in general use is for a primary term and "as long thereafter as oil and gas, or either of them, is produced from the lands by the lessee."

3. *The Issue of Paying Quantities*

When one thinks of the construction that has been given the habendum clause in some jurisdictions, he is likely to be reminded of that bit of verse that goes like this: "As I was going up the stair I met a man who wasn't there. He wasn't there again today, I wish, I wish he'd stay away." This feeling is brought on by two words you will not find in the usual habendum clause, but they are there just the same.

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[56] Walker, *The Nature of the Property Interest Created by an Oil and Gas Lease in Texas*, 11 TEXAS L. REV. 339, 402 (1933).

[57] MERRILL, COVENANTS IMPLIED IN OIL AND GAS LEASES 463 (2d ed. 1940).

[58] See, *e.g.*, French v. Haldeman, 53 Pa. 229 (1867).

[59] See, *e.g.*, Union Petroleum Co. v. Bliven Petroleum Co., 72 Pa. 173 (1872).

[60] See, *e.g.*, Dark v. Johnston, 55 Pa. 164 (1867).

[61] See 2 SUMMERS, *op. cit. supra* note 36, § 230 at 105.

Furthermore, it would not do any good to wish they would go away, even if that were desired, for it appears they are with us permanently, at least in some jurisdictions. These two words are: "paying quantities."

In the early days of the oil and gas industry the habendum clause usually provided that the lease should extend for a specified period and "as long thereafter as oil or gas is produced *in paying quantities.*"[62] In the later lease forms the words "paying quantities" are omitted from the habendum clause. Practically all modern lease forms provide only that the lease shall extend for a definite term and as long thereafter as oil or gas, or either of them, "is produced." Often the omission of words formerly used in a contract and later deleted from the contract form is given serious consideration in construing the contract, as we shall see later. However, some of the courts, including those of Texas and Oklahoma, give no recognition to the change and make no distinction between the words "is produced" and "is produced in paying quantities." They say the word "produced" means "produced in paying quantities,"[63] although the dictionary has failed to include any such definition of the word "produce." There is no element of "paying" or "profit" inherent in the word "produce" according to *Webster's International Dictionary*. Other courts have held that the "strict letter of the lease is complied with" although "the quantity produced was so small as to make the venture unprofitable."[64]

The Supreme Court of Mississippi has taken a very definite stand on this issue. In *Roberts v. Corum*[65] the Supreme Court of this state construed a clause in a lease that provided "if after the discovery of oil, gas or other mineral, the *production* thereof should cease for cause" the lease should not terminate, if within the primary term, provided the payment of rentals should be resumed or operations for drilling or reworking be commenced on or before the rental paying date next ensuing after the expiration of 60 days from the cessation of production. The court said:

> The basic contention of the appellants is that applying Paragraph 6 of the Corum lease hereinbefore quoted, the said lease expired by its terms, because the appellees failed to commence drilling or reworking operations *within 60 days after cessation* of production, and that the word "production" as used in the lease *means production in paying quantities.*[66] (Emphasis added.)

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[62] See, *e.g.*, Roach v. Junction Oil & Gas Co., 72 Okla. 213, 179 Pac. 934 (1919).

[63] *E.g.*, Gypsy Oil Co. v. Marsh, 121 Okla. 135, 248 Pac. 329 (1926), 48 A.L.R. 876 (1927); Garcia v. King, 139 Tex. 578, 164 S.W.2d 509 (1942).

[64] *E.g.*, Enfield v. Woods, 198 Ky. 328, 248 S.W. 842 (1923); South Penn Oil Co. v. Snodgrass, 71 W. Va. 438, 76 S.E. 961 (1912), 43 L.R.A. (n.s.) 848 (1913).

[65] 236 Miss. 809, 112 So. 2d 550 (1959).

[66] *Id.* at 819, 112 So. 2d at 553.

There was a well which produced continuously until reworking operations were commenced, but not in paying quantities. On the issue of what "production" means, Judge Holmes stated:

> There is nothing in the lease providing for its expiration for the failure of the lessee to produce oil or gas in *paying quantities* during the primary term of the lease. There is nothing ambiguous in the use of the word "production" and we are not authorized to enlarge upon it, or detract from it, or to ascribe to it a meaning which the parties themselves did not see fit to ascribe to it. . . . If the parties had intended that the word "production" should mean production in paying quantities it would have been a very easy thing to write that into the lease. They did not see fit to do so. Contracts are solemn obligations and it is not the function of the courts to make contracts for parties, but rather to give effect to them as written.[67]

I submit that is sound logic and correct legal reasoning.

As to the rule adopted by the Supreme Courts of Texas and Oklahoma, a little judicial history is interesting. The case of *Garcia v. King*,[68] decided in 1942 by the Supreme Court of Texas, followed the Oklahoma decision of *Gypsy Oil Co. v. Marsh*,[69] decided in 1926. In the *Marsh* case the Supreme Court of Oklahoma, in holding that "produced" means "produced in paying quantities," said it was committed to that doctrine by the earlier Oklahoma case of *Parks v. Sinai Oil Company*.[70] Yet an examination of the opinion in the *Sinai* case will show how weak it is as an authority for construing the word "produced" as meaning "produced in paying quantities." There a well had been drilled and the issue was whether there was production in paying quantities before the expiration of the primary term. A well had been completed within that period. It was not productive in paying quantities in a lower sand in which it was completed, but the court found, from sharply conflicting evidence, that gas had been discovered in paying quantities in an upper sand during the drilling of the well, and that discovery satisfied the lease requirement of production. There was no direct issue as to whether "produced" means "produced in paying quantities" for the reason that the habendum clause of the lease provided for a term and so long thereafter as oil or gas was produced "in paying quantities," and the court found that the production was in paying quantities. Hence, there was no occasion for construing the word "produced." Yet, the Texas, Montana, and later Oklahoma holdings are based on the *Marsh* case, and the *Marsh* case in turn rests upon the *Sinai* case. All this is purely academic, of course, but it is interesting to observe how a rule of case law sometimes gets started.

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[67] *Id.* at 822, 112 So. 2d at 554.

[68] 139 Tex. 578, 164 S.W.2d 509 (1942).

[69] 121 Okla. 135, 248 Pac. 329 (1926), 48 A.L.R. (1927).

[70] 83 Okla. 295, 201 Pac. 517 (1921).

a. *What Constitutes "Paying Quantities"*

There are two definitions of "paying quantities." One is used where the issue is whether the lessee is required to drill in order to protect the leased premises from drainage by wells on adjoining acreage. In such case it must be shown that a well on the leased premises would be sufficiently productive to pay the lessee a profit over and above drilling and operating costs.[71]

On the other hand, a lease may be continued in force under the "thereafter" clause of the habendum provision if it will pay a profit to the lessee over and above the cost of operating the well or wells, even though the cost of drilling and equipping the well or wells may never be recovered.[72]

The difficult question is to determine the factors that are to be considered in deciding whether production in paying quantities actually exists. Probably the leading case on this issue is the late Texas case of *Clifton v. Koontz*.[73] This case first discussed the period of time to be used in determining whether there is deficit in income over operating expenses. The lessor had contended that a sixty-day period, based on a clause in the lease, should be used, but the court refused to follow that contention. It said there "can be no arbitrary period . . . for the additional reason that there are various causes for slowing up production, or a temporary cessation of production, which the courts have held to be justifiable."[74] The period, therefore, depends upon the circumstances of each case.

Further, in the *Koontz* opinion the court emphasizes that there may be conditions affecting the determination of "paying quantities" other than money received or paid, as per the following paragraphs from the opinion:

> In determining paying quantities, in accordance with the above standard, the trial court necessarily must take into consideration all matters which would influence a reasonable and prudent operator. Some of the factors are: the depletion of the reservoir and the price for which the lessee is able to sell his produce, the relative profitableness of other wells in the area, the operating and marketing costs of the lease, his net profit, the lease provisions, a reasonable period of time under the circumstances, and whether or not the lessee is holding the lease merely for speculative purposes.

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[71]See, *e.g.*, Coyle v. North Am. Oil Consol., 201 La. 99, 9 So. 2d 473 (1942); Texas Pac. Coal & Oil Co. v. Barker, 117 Tex. 418, 6 S.W.2d 1031 (1928), 60 A.L.R. 936 (1929).

[72]See, *e.g.*, Knight v. Blackwell Oil & Gas Co., 197 La. 237, 1 So. 2d 89 (1941); Walden v. Potts, 194 Okla. 453, 152 P.2d 923 (1945); Garcia v. King, 139 Tex. 578, 164 S.W.2d 509 (1942).

[73]160 Tex. 82, 325 S.W.2d 684 (1959).

[74]325 S.W.2d at 690.

> The term "paying quantities" involves not only the amount of production, but also the ability to market the product (gas) at a profit. See Benedum-Trees Oil Co. v. Davis, 107 F. 2d 981, and Hanks v. Magnolia Petroleum Co. (Tex. Com. App.), 24 S.W. 2d 5. Whether there is a reasonable basis for the expectation of profitable returns from the well is the test.[75]

Following the above quotation the court named other factors that must be considered with a discussion of each. They are: (1) *Action of regulatory bodies* in fixing the rate of production; (2) *Depreciation of the original investment cost,* the court holding that such depreciation should not be taken into consideration as a part of the expense in operating the well; (3) *Deduction of overriding royalties in fixing lessee's income.* The court held that the "entire income attributable to the contractual working interest created by the original lease is to be considered", and (4) *Good faith of the operator.* As to this the court said:

> In the case of a marginal well, such as we have here, the standard by which paying quantities is determined is whether or not under all the relevant circumstances a reasonable prudent operator would for the purpose of making a profit and not merely for speculation, continue to operate a well in the manner in which the well in question was operated.[76]

Other authorities on the "good faith" issue are abundant.[77]

b. *"Paying Quantities": A New Application of the Principle*

In the case of *Gypsy Oil Co. v. Marsh*[78] and other cases involving the term "paying quantities" as used in the habendum clause, the issue was to give the lessor relief by terminating the lease. In a recent Oklahoma case the situation is presented in reverse.[79] The rule invoked is the same, but the remedy sought is hardly recognizable. In this case the

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[75]*Id.* at 691.

[76]*Ibid.*

[77]See, *e.g.,* Reynolds v. White Plains Oil & Gas Co., 199 Ky. 243, 250 S.W. 975 (1923); Bay State Petroleum Corp. v. Penn Lubricating Co., 121 Ky. 637, 87 S.W. 1102 (1905); Texas Pac. Coal & Oil Co. v. Bruce, 233 S.W. 535, 539 (Tex. Civ. App. 1921) where the court said: "Numerous other authorities might be cited in support of the rule that the stipulation that the lease shall continue so long as oil or gas is found in 'paying quantities' is a stipulation for the benefit of the lessee, and that the lessee may in good faith exercise his judgment as to whether he shall continue operation or abandon the lease, but we think sufficient have been cited." *Accord,* Aycock v. Paraffin Oil Co., 210 S.W. 851 (Tex. Civ. App. 1919); Masterson v. Amarillo Oil Co., 253 S.W. 908 (Tex. Civ. App. 1923), where it is said: "The courts hold that the question of what amounts to oil and gas in paying quantities is a matter to be determined exclusively by the lessee acting in good faith."

[78]121 Okla. 135, 248 Pac. 329 (1926).

[79]Gallaspy v. Warner, 324 P.2d 848 (Okla. 1958).

lessor protested the lease termination, and alleged that the lease could continue in profitable operation even though the lessee, after reworking operations on the wells, claimed that production could not be obtained in paying quantities. Damages were sought by the reversionary owner. The plaintiff presented one petroleum engineer who testified that, in his opinion, the well could produce 56,000 barrels of "economically recoverable oil." The court said: "There was a conflict between the testimony and opinions of the engineer, Dooley, and that of the *engineers* who testified on behalf of the defendant Gallaspy *with respect to the amount of recoverable oil under the well and the cost of producing the same. . . .*"[80] (Emphasis added.) But it held that the testimony of plaintiff's one engineer was sufficient to constitute a preponderance and sustain the burden of proof as against the testimony of the "engineers" offered by the defendant, and judgment was rendered against the operator. The trial court found that there were 30,000 barrels of "economically recoverable oil" instead of 56,000 barrels as testified by plaintiff's engineer. The "economics" by which the amount was determined is not stated. There is not a word in the opinion about the cost of production or how it was computed. The court merely said that the well would produce 200 barrels a month "when efficiently operated" for a period of twelve and one-half years. It also found the price of oil would be $2.50 per barrel for that period. The trial court's judgment was for $9,375, plus $387.45, interest on past due royalty. The supreme court, however, reduced the judgment to $7,886.70 by discounting royalty installments "not yet due," stating that otherwise the plaintiff "would receive the use of the money in advance of the time he was entitled to recover it."[81]

4. *Actual Production Necessary to Extend Lease Beyond Primary Term*

The majority of the courts in the various oil and gas producing states have held that where a lease provides that it shall continue in force for a certain term of years and as long thereafter as oil or gas is produced from the land, production must be obtained before the expiration of the primary term in order to continue the lease in force. Particularly is this true in the "ownership in place" states where an oil and gas lease is held to be a "determinable fee" and "determines" at the expiration of the primary term if the lease is not producing.[82] Other states in which the rule has been announced that a lease expires if

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[80] *Id.* at 852.

[81] *Id.* at 853.

[82] See, *e.g.*, Normandie Oil Corp. v. Oil Trading Co., 139 Tex. 402, 163 S.W.2d 179 (1942).

production is not obtained before expiration of the primary term are Illinois,[83] Indiana,[84] Kansas,[85] Louisiana,[86] Michigan,[87] Montana,[88] New Mexico,[89], Ohio,[90] Pennsylvania,[91] and West Virginia.[92]

In Oklahoma the rule is different. There the supreme court has construed the habendum clause together with the rental clause, and the Oklahoma rule is that if a well is commenced during the last rental period for which rental has been paid, such well may be drilled to completion, even though not completed until after the expiration of the primary term; and if such drilling results in the discovery of oil and gas the lease will continue in force as long as oil or gas is produced in paying quantities. The basis of this holding is that when the rental is paid for the last year of the lease, the lessee is given the right to commence a well at any time during the year, even on the last day thereof. Such a right, said the courts, contemplates the further right to *complete* that which was allowed to commence.[93]

5. *Extension of Term Based on Lack of Market and Other Equitable Considerations*

In jurisdictions where the "determinable fee" principle is not applied it is generally the rule that where a well, capable of producing in paying quantities, is drilled and completed within the primary term but the operator is unable to market the product immediately on account of lack of an available market or pipe line connections, the lease

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[83]See Carter Oil Co. v. Liggitt, 371 Ill. 482, 21 N.E.2d 569 (1939); Poe v. Ulrey, 233 Ill. 56, 84 N.E. 46 (1908).

[84]See Chaney v. Ohio & Ind. Oil Co., 32 Ind. App. 193, 69 N.E. 477 (1904).

[85]See Perkins v. Saunders, 109 Kan. 372, 198 Pac. 954 (1921); Baldwin v. Blue Stem Oil Co., 106 Kan. 848, 189 Pac. 920 (1920); Elliott v. Crystal Springs Oil Co., 106 Kan. 248, 187 Pac. 692 (1920).

[86]See Parten v. Webb, 197 La. 197, 1 So. 2d 76 (1941); Talley v. Lawhon, 150 La. 25, 90 So. 427 (1922); Cooke v. Gulf Ref. Co., 127 La. 592, 50 So. 874 (1910).

[87]See Kinne v. Swanson Consol. Oil Co., 293 Mich. 509, 292 N.W. 472 (1940).

[88]See Berthelote v. Loy Oil Co., 95 Mont. 434, 28 P.2d 187 (1933).

[89]See Town of Tome Land Grant v. Ringle Dev. Co., 56 N.M. 101, 240 P.2d 850 (1952).

[90]See Tedrow v. Shaffer, 23 Ohio App. 343, 155 N.E. 510 (1926); Murdock-West Co. v. Logan, 69 Ohio St. 514, 69 N.E. 984 (1904).

[91]See Cassell v. Crothers, 193 Pa. 359, 44 Atl. 446 (1899); Shellar v. Shivers, 171 Pa. 569, 33 Atl. 95 (1895).

[92]See Anderson v. Schaffner, 90 W. Va. 225, 110 S.E. 566 (1922); Eastern Oil Co. v. Coulehan, 65 W. Va. 531, 64 S.E. 836 (1909).

[93]See McClain v. Harper, 206 Okla. 437, 244 P.2d 301 (1952); Simons v. McDaniel, 154 Okla. 168, 7 P.2d 419 (1932); Dow v. Worley, 126 Okla. 175, 256 Pac. 56 (1926). The Oklahoma cases followed Lester v. Mid-South Oil Co., 296 Fed. 661 (6th Cir. 1924), a case arising in Kentucky, and the Kentucky Supreme Court has also announced the same rule. Simpson v. Buckner's Adm'r., 247 Ky. 567, 57 S.W.2d 464 (1933).

will not terminate if the operator exercises due diligence in seeking a market, and the market is found within a reasonable time.[94]

In some lease forms the habendum clause is for a definite term of years with the further provision that in case oil or gas is "discovered" on the premises the lease shall continue thereafter so long as "production" is obtained in paying quantities. The issue was thus presented as to whether "discovery" is synonymous with "production." In Texas the courts hold that the two words are not synonymous. In one case where the word "discovered" was used in the habendum clause, the court held that "the lessee, in common fairness and justice, was entitled to a reasonable length of time within which to continue the development work."[95] In a later Texas case where the habendum clause was for five years and as long as "oil or gas is produced," the court held that where production was not obtained prior to the expiration of the primary term, the lease terminated.[96] It applied the same principle as that applied in the *Bratton* case, that "discovery" is not synonymous with "production." Other Texas cases have applied this rule.[97] However, another Texas case did hold that where gas was discovered within the primary term the lessee should have a "reasonable time to market the gas"; but it defined "reasonable time" as the "reasonable time it would take appellant to lay a line from its well to the only available market."[98]

C. The Royalty Clauses

There has been little change in the oil royalty clause throughout the years. The lessee agrees to deliver the royalty oil to the lessor in the pipe line to which the lessee connects his wells. The purchaser of the oil usually makes separate payments to the lessee and the royalty owner. Sometimes the lease provides that the lessee may purchase the royalty oil at the prevailing market price. Again, there are cases where the lease provides that the royalty owner may take his oil "in kind" and not sell it to the lessee's purchaser. In such cases the lease usually provides that the lessor must furnish the tanks or pipe lines necessary to receive the royalty oil. It has been held that where the lessor failed to provide tanks or a pipe line to receive the royalty oil the lessee had the right to deliver it in the pipe line to which lessee connected its wells.[99]

In the event the lessor does not take his oil in kind, the responsi-

[94]See, *e.g.*, Pennegrade Oil & Gas Co. v. Martin, 211 Ky. 137, 277 S.W. 302 (1925); Strange v. Hicks, 78 Okla. 1, 188 Pac. 347 (1920).

[95]Texas Pac. Coal & Oil Co. v. Bratton, 239 S.W. 688 (Tex. Civ. App. 1921).

[96]Morrison v. Swaim, 220 S.W.2d 493 (Tex. Civ. App. 1949).

[97]See, *e.g.*, Continental Oil Co. v. Boston-Texas Land Trust, 221 F.2d 124 (5th Cir. 1955); Holchok v. Clark, 284 S.W.2d 399 (Tex. Civ. App. 1955).

[98]Union Oil Co. v. Ogden, 278 S.W.2d 246 (Tex. Civ. App. 1955).

[99]See Sohio Petroleum Co. v. United States & P.R.R., 222 La. 383, 62 So. 2d 615 (1952), *appeal dismissed*, 346 U.S. 802 (1953).

bility to market the production is upon the lessee. As said in a leading case, "In the absence of an express provision in an oil and gas lease with respect to marketing the production, there is an implied duty on the part of the lessee to make diligent efforts to market the production in order that the lessor may realize on his royalty interest."[100] Other cases on this point are numerous.[101]

Where there is no pipe line connection available at the well, and the oil produced must be transported by truck to the nearest market or pipe line, one case has held that the lessor should pay the reasonable charges for such transportation of this royalty oil. [102]

In the early days of the industry when gas was just a nuisance product encountered in the search for oil, a gas royalty of one to two hundred dollars per year was considered adequate, and most leases contained such clauses. With the increased demands and uses for gas, and products processed from gas, the gas royalty clauses were changed usually to a percentage of one-eighth of the gas produced, or its value. A form of gas royalty clause in common use was as follows: "Where gas only is found, one-eighth of the value of all raw gas at the mouth of the well, while said gas is being used or sold off the premises, payment for gas so used or sold to be made monthly." This clause appeared sufficient where dry gas was produced from a gas well and was delivered to pipe lines that connected with the wells. Later, however, the production of "wet gas" brought on new problems.

First, there was "casinghead gas," which is gas produced from an oil well, and otherwise defined as "any gas and/or vapor indigenous to an oil stratum and produced from such stratum with oil."[103] The Texas courts have held that casinghead gas is oil, and royalty thereon is payable under the oil royalty clause.[104] The basis of the Texas holding is that the "constituent elements" or "component parts" of casinghead gas are also found in oil, and this reasoning is often referred to as the "component part" theory, and has been followed in other states.[105]

The Supreme Court of Oklahoma has treated casinghead gas differently from the holdings in other jurisdictions. It holds that casinghead gas is neither gas nor oil, but is a substance different from either,

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[100]Wolfe v. Prairie Oil & Gas Co., 83 F.2d 434, 437 (10th Cir. 1936).

[101]See, *e.g.*, Phillips Petroleum Co. v. Peterson, 218 F.2d 926 (10th Cir. 1954); Cole Petroleum Co. v. United States Gas & Oil Co., 121 Tex. 59, 41 S.W.2d 414 (1931).

[102]Molter v. Lewis, 156 Kan. 544, 134 P.2d 404 (1943).

[103]1 SUMMERS, OIL AND GAS 258 (perm. ed. 1954).

[104]See, *e.g.*, Gilbreath v. States Oil Corp., 4 F.2d 232 (5th Cir. 1925); Livingston Oil Corp. v. Waggoner, 273 S.W. 903 (Tex. Civ. App. 1925).

[105]See, *e.g.*, MacNicol v. East Coalingo Oil Fields Corp., 122 P.2d 661 (Cal. App. 1942), *modified and aff'd*, 22 Cal. 2d 742, 140 P.2d 793 (1943); Wemple v. Producing Oil Co., 145 La. 1031, 83 So. 232 (1919); Locke v. Russell, 75 W. Va. 602, 84 S.E. 948 (1915).

and that a lease where royalty clauses cover only "gas" and "oil" as such, does not cover casinghead gas.[106] The basis of the holding was that the lease for oil and gas "means oil in its ordinary acceptation and gas from a gas well as the same is ordinarily understood," applying an Oklahoma statute on construing contracts generally.[107] The "component part" or "constituent element" theory, applied in Texas, was rejected in Oklahoma. However, a lease that provided for a royalty on "gas produced from an oil well" was held to cover casinghead gas.[108]

In later years, another product called "condensate" has been found and produced from deep gas wells. Condensate is produced as a liquid but it exists in a gaseous state in the reservoir. This reservoir condition is occasioned by high temperatures and great pressures. Upon reduction of the temperature and pressure by ordinary production methods the condensate liquefies and falls out of the gas in the separators at the mouth of the well. This process is called "retrograde condensation." The issue, then, is whether "condensate" is to be classified as oil, or gas, or neither, under the royalty clauses of the usual oil and gas lease.

This question was first raised in Texas in the case of *Lone Star Gas Co. v. Stine*.[109] There the issue revolved about the construction of a deed in favor of Lone Star Gas Company conveying "all natural gas." It was contended by the appellee that "condensate" contained the same hydrocarbons as oil and was therefore to be considered as "oil" under the "constituent element" case of *Reynolds v. McMan Oil Co.*[110] However, the court, without reference to the *McMan* case, held that the "term 'all natural gas' would include all the substances that come from the well as gas, and that regardless of whether such gas be wet or dry."[111] Apparently, the court overlooked the fact that condensate does not "come from the well" as gas, but as a liquid. It would seem that the court would have been on a sounder basis if it had held that the product "condensate" exists in a gaseous state in the reservoir and that in Texas, where the "ownership in place" doctrine prevails, the owner of the gas rights acquired his title to the substance while it was still in the reservoir. Three other Texas cases have construed the words "gas only" in an oil and gas lease, and have held that "condensate" is a "constituent

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[106]See, *e.g.*, Broswood Oil Co. v. Sand Springs Home, 178 Okla. 550, 62 P.2d 1004 (1936); Hammett v. Gypsy Oil Co., 95 Okla. 235, 218 Pac. 501 (1921), 34 A.L.R. 275 (1921).

[107]*Ibid.*

[108]See Musselin v. Magnolia Petroleum Co., 107 Okla. 183, 231 Pac. 526 (1924).

[109]41 S.W.2d 48 (Tex. Comm'n App. 1931).

[110]11 S.W.2d 778 (Tex. Comm'n App. 1928), *aff'd on rehearing*, 14 S.W.2d 819 (1929).

[111]11 S.W.2d at 782.

element" of gas and therefore is included in the gas royalty clause of a lease.[112]

In a recent case, arising in Texas and decided by the Court of Appeals for the Fifth Circuit, the court had under consideration a case where there was a gas well which produced condensate.[113] The lessee was forced to shut in the well for lack of market for the gas. There was a "shut-in" gas clause in the lease which read: ". . . where gas from a well producing gas only is not sold or used Lessee may pay as royalty $50.00 per well per year, and upon such payment it will be considered that gas is being produced within the meaning of Paragraph 2 hereof."[114] The court held that the lessee could not avail itself of the shut-in provision. It refused to accept the definition of "gas only" as given in the four Texas cases referred to. The *Goodroe* case was practically identical in facts with this case. It held that the shut-in clause applied and that *"the well was producing gas only from which a certain amount of condensate, a component part of the gas* was being extracted and sold."[115] (Emphasis added.)

Nevertheless, the Court of Appeals did not mention nor even refer to the *Stine, Harris, Poe* or *Goodroe* cases in the majority opinion. It held that condensate "is *not therefore gas* within the intendment of the constructive production provision." It then ordered the lessee "to produce liquid condensate alone" and then advised lessee how it could be done. The method prescribed by the court was by "such an operation . . . known in the industry as cycling." Of course, there is much more to cycling than drilling two wells and producing condensate from one and using the other as an input well for gas. Cycling is a complex operation, intended to conserve, preserve and increase future operations in a wide area. There can be no effective cycling with just two wells. In fact, the publication, *Petroleum Conservation*, published by the American Institute of Mining and Metallurgical Engineers, states that there can be no really efficient cycling operation except in a unit operation, involving the complete reservoir, and this feature was presented to the court.[116] It should be said that one of the three judges, Judge Jones, dissented. He cited the four Texas cases above mentioned and said: "It does not seem to me there is anything in the instrument before the court that permits of a construction that 'gas only' may mean only dry gas."[117]

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[112]See Shell Oil Co. v. Goodroe, 197 S.W.2d 395 (Tex. Civ. App. 1946); Humble Oil & Ref. Co. v. Poe, 295 S.W.2d 1019 (Tex. Comm'n App. 1930); Lone Star Gas Co. v. Harris, 45 S.W.2d 664 (Tex. Civ. App. 1923).

[113]Vernon v. Union Oil Co., 270 F.2d 441 (5th Cir. 1959).

[114]*Id.* at 442.

[115]197 S.W.2d at 397.

[116]270 F.2d at 446.

[117]*Id.* at 447.

In 1938 the Supreme Court of the United States handed down what was then called one of its great epoch-making decisions, *Erie Railroad Co. v. Tompkins*,[118] which overruled the prior decision of *Swift v. Tyson*.[119] In the *Erie* case the court held: (1) "There is no federal general common law," and (2) "Except in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the state." One wonders, sometimes, whether some of our federal courts have overlooked or forgotten the *Erie* case, or perhaps reached the conclusion that it is outmoded and obsolete. It does appear that Mr. Justice Frankfurter once was deciding a case when some old cases got in his way, and he disposed of them by saying they had been worn away "by the erosion of time." However, so far as this writer knows, that doctrine has not yet been applied to the *Erie* case. Instead, *Erie* has been followed faithfully by most of the federal courts in hundreds of decisions.

An interesting case from Oklahoma on whether condensate is covered by a lease which grants the right to drill for and produce oil and gas only is the case of *Mid-Continent Petroleum Corporation v. Blackwell Oil & Gas Co.*[120] In that case the plaintiff, Mid-Continent, was the owner of the oil rights and the defendant the owner of the gas rights under one oil and gas lease. A gas well was drilled on the leased premises and it produced a considerable amount of liquid, which was recovered in a "drip" located between the well and the gas meter. The issue was whether the owner of the gas rights was entitled to the recovered liquids as a part of the gas. The Supreme Court of Oklahoma held that the liquids were not a part of the gas. It reviewed the casinghead gas cases and the basis for holding that casinghead gas, or gas from an oil well, was neither oil nor gas. In its opinion it said: "In the Mussellem case it was pointed out that the contract therein involved dealt with *oil produced and saved, gas produced and saved from a gas well, and gas produced and saved from an oil well. Herein is involved a fourth element—gasoline coming from a gas well.*"[121] (Emphasis added.) The royalty provisions of the lease were not involved, but the reasoning of the court would indicate that a lease with royalty clauses covering only oil, gas and casinghead gas would not include that "fourth element" which the court calls "readily condensible gasoline" produced from a gas well.

Another, and fairly recent provision, in the gas royalty paragraph applies to "shut-in" wells. Where there is no market for gas near the source of production, or for conservation purposes or other reasons,

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[118]304 U.S. 64 (1938), 114 A.L.R. 1487 (1939).

[119]16 Pet. (14 U.S.) 1 (1842).

[120]159 Okla. 35, 15 P.2d 1028 (1932).

[121]15 P.2d at 1035.

such wells cannot be produced, a lease may be continued in force by the payment of a "shut-in" royalty which shall continue the lease in force for specified periods, and during the time such "royalty" payments are made it "shall be considered that gas is being produced from the leased premises in paying quantities," as required by the habendum clause of the lease.

The courts have exhibited a tendency to construe this clause strictly. In a Texas case where a well was completed near the end but before the expiration of the primary term, the "shut-in" payment was not made until shortly after the term expired.[122] The court held that the lease lapsed because there was no "producing well" on the premises at the time the primary term expired. In other words the gas well could not be considered a "producing well" under the "shut-in" clause at the time it was *shut in*; that status could not occur until payment of the "shut-in" royalty.[123]

The late Texas case of *Gulf Oil Corporation v. Reid*[124] was another controversial decision. The lease contained a clause providing for drilling or reworking operations after the expiration of the primary term. It also contained the usual "shut-in" royalty clause, providing that by an annual payment of fifty dollars it would be considered a producing well within the meaning of the habendum clause. A gas well was completed *after* the expiration of the primary term and the shut-in royalty tendered within "a reasonable time" thereafter, as found by the trial court. However, the Supreme Court reversed the case, holding that the "shut-in" payment had been made after the well "had been capped," and therefore the lease terminated. The decision would seem to require that a lessee, completing a well after the expiration of the primary term, should have a purchaser's lines ready to connect with the lease on the day of completion, or to pay the shut-in royalty on that day. The capping of the well would seem to be the act that would terminate the lease, if the shut-in royalty has not been paid prior to or on the date of capping.

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122 Freeman v. Magnolia Petroleum Co., 141 Tex. 274, 171 S.W.2d 339 (1943).

123See SOUTHWESTERN LEGAL FOUNDATION, SEVENTH ANNUAL INSTITUTE ON OIL AND GAS LAW AND TAXATION 47 (1956), where a former justice of the Supreme Court of Texas criticizes the opinion in the *Freeman* case. He calls it an "instance of the Court's paying more attention to the justice of the result than to the form of the obligation. . . ." He says the case "involved the remedy for breach of an express covenant to pay royalty" and cited authority that "usually the breach of an express covenant to pay royalty would permit only the remedy of the recovery of damages." However, Professor Walker takes the position that the payments under the "shut-in" clause were "in lieu of production" and as a "substitute for production" and thus are tied into the habendum clause. See Walker, *Clause in Oil and Gas Leases Providing for the Payment of an Annual Sum as Royalty on a Nonproducing Gas Well*, 24 TEXAS L. REV. 478, 480 (1946).

124161 Tex. 51, 337 S.W.2d 267 (1960).

In a case arising in Mississippi the "shut-in" clause was applied to a situation where a portion of a lease had been assigned to others, and the question was whether a well completed on the reserved portion operated to continue the lease in force as to all the acreage originally contained therein.[125] The court held that the well and payment of the "shut-in" royalty was effective to continue the entire lease in force.

The issue has arisen in cases where "royalty" only is owned under a lease as to whether the "royalty" owner is entitled to participate in payments of "shut-in" royalty. This situation has appeared in cases where a mineral owner, who owns less than the entire mineral interest in a certain tract of land, has the exclusive leasing rights, sometimes called the "executive rights," and is entitled to receive the entire amounts of bonus and delay rentals. As to "shut-in" royalty payments, however, courts have announced a different rule. While royalty has been defined as a share of the product of the well, nevertheless, because the "shut-in" payment is denominated as "royalty" and is "in the nature of minimum royalty payments," the royalty owner is entitled to share in such payments.[126]

D. The Rental Clause

The so-called rental, as provided in an oil and gas lease, is not really a rental at all within the real meaning of the word. A rental has been defined as a fixed sum to be paid at stated times for the use of property.[127] The rental in an oil and gas lease is not payment for the *use* of property; it is commutation money paid for the privilege of postponing the drilling and development of the leased property.

In the early days there were no provisions for payment of rentals in oil and gas leases. These leases required immediate development. It was thought then that oil and gas underlying lands were capable of migrating freely from one tract to another whether or not there were producing wells on other tracts causing "drainage" as we know it today. Thus, a lessee could not take a lease until he was ready to drill on it. This, of course, would prevent lessees from taking blocks of acreage for future development. In the leases in which rental clauses first appeared, there was a "drill or pay" provision, followed by a forfeiture clause, which rendered a lease null and void if drilling was not commenced or the rental paid.

Next, there appeared a lease form which provided that the lessee should drill within a certain time or pay a stipulated sum as rental which would postpone the obligation to drill for a stated period (usu-

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[125]Bery v. Tidewater Associated Oil Co., 188 F.2d 820 (5th Cir. 1951).

[126]See, *e.g.*, Carlisle v. United Producing Co., 278 F.2d 893 (10th Cir. 1960); *accord,* Morris v. First Nat'l Bank, 249 S.W.2d 269 (Tex. Civ. App. 1952).

[127]See Duffy v. Central R.R., 268 U.S. 55 (1925).

ally one year) without an express provision for forfeiture in the event the lessee failed either to drill or pay. Where a drilling clause of this type was used it was held in most jurisdictions that the lessor did not have the right to terminate the lease. His remedy was to bring an action for the recovery of the rental.[128]

Prior to 1916 there was in Oklahoma a new development in connection with the duty to pay rentals. It was the introduction into the lease of the "surrender" clause, which provided that the lessee should have the right at any time to surrender the lease to the lessor and be discharged from any further obligation thereunder. Usually the exercise of the surrender privilege called for the payment of a nominal sum, usually one dollar. Then came the case of *Brown v. Wilson*,[129] where the Supreme Court of Oklahoma held that because the surrender clause in the lease "rendered the performance thereof optional as to the lessee . . . it was also optional as to the lessor," and the lessor could also terminate the lease in the same manner as the lessee. However, within two years the Supreme Court of Oklahoma reversed *Brown v. Wilson* in the case of *Rich v. Doneghey*.[130] Notwithstanding the reversal of *Brown v. Wilson,* the "drill or pay" lease, ordinarily called the "or" lease, fell into disuse and was superseded by the "unless" lease.[131]

E. The "Unless" Rental Clause

Shortly after the decision of the Supreme Court of Oklahoma in *Brown v. Wilson,* several Tulsa attorneys, headed by James A. Veasey of Carter Oil Company, and James B. Diggs of Gypsy Oil Company, Gulf subsidiary, got together to find a substitute for the lease form containing a "surrender" clause. They came up with the "unless" provision in the rental clause. A typical form of this clause is:

> If no well be commenced on said land on or before the_____ day of _____, 19____, this lease shall terminate as to both parties *unless* the lessee on or before that date shall pay or tender to the lessor, or to lessor's credit in the _____ Bank, at _____, or its successors . . . the sum of _____ Dollars, which shall operate as a rental and cover the privilege of deferring the commencement of a well for _____ months from said date.

Then followed a clause giving the lessee the right to defer the com-

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[128]See, *e.g.,* Jackson v. Twin State Oil Co., 95 Okla. 96, 218 Pac. 324 (1923); Collins v. Humble Oil & Ref. Co., 223 S.W. 696 (Tex. Civ. App. 1920).

[129]58 Okla. 392, 160 Pac. 94 (1916).

[130]71 Okla. 204, 177 Pac. 86 (1918), 3 A.L.R. 352.

[131]Other states did not have the difficulty experienced by the Oklahoma court in determining the effect of the "surrender" clause. It is generally held that a lease is not unilateral merely because it contains a clause providing for its surrender by the lessee. See, *e.g.,* Lindlay v. Raydure, 239 Fed. 928 (E.D. Ky. 1917).

mencement of a well for like periods thereafter by the payment of the same amounts of rental in the same manner.

This form of lease was taken by its authors to the Burkhart Printing Company in Tulsa for printing, and when it came out there appeared at the top of the lease the words "Producers 88." That appellation has remained in most oil and gas lease forms since the first one was published. In recent years oil and gas attorneys have engaged in research in order to ascertain the significance of "88" in naming the lease form. The best explanation, it appears, was that the Burkhart Company numbered consecutively the different forms it printed and this lease form happened to be number 88. In any event, most lease forms today bear the number "88" in some relationship. Often other words are added, such as "Producers 88 Revised," "Producers 88 Special," "Producers 88 with Pooling," etc. Often Bill Jones, a broker, would add to or change a few words in the original form and proudly name it "Producers 88—Bill Jones."

One of the first questions that arose in the "unless" provision was, What is the commencement of a well? Does it mean that the well must actually be drilling, making hole, before it is a commencement? The general rule seems to be that actual drilling is unnecessary. It is sufficient if preparations for drilling, such as moving in drilling equipment, erecting a derrick, digging the cellar, and operations of that kind are commenced on or before the date required.[132] However, the preparatory operations will not constitute a commencement unless the lessee exercises diligence and good faith in commencing the actual drilling.[133]

In Montana a distinction has been made between a lease which provides for the commencement of *operations* for drilling and one which requires the commencement of *drilling* by a certain time; and it was held that where the lessee is required to "commence drilling" there must be actual drilling on that date to comply with the lease provisions.[134] This is the minority rule.

Another question that has arisen is how the rental should be paid. Should the rental be paid or tendered in actual money, sufficient to constitute a legal tender? It has been held that where a check is tendered in payment of a rental and drawn on a bank in which the drawer has sufficient funds, the payment is good if timely objection is not

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[132]See, *e.g.*, Vickers v. Peaker, 227 Ark. 587, 300 S.W.2d 29 (1957); Aldridge v. Gypsy Oil Co., 132 Okla. 13, 268 Pac. 1109 (1928); McCallister v. Texas Co., 223 S.W. 859 (Tex. Civ. App. 1920).

[133]See, *e.g.*, Niles v. Mead, 189 Ky. 243, 224 S.W. 854 (1920); Hudspeth v. Producers Oil Co., 134 La. 1013, 64 So. 891 (1914); Dunbar v. Fuller, 253 S.W.2d 684 (Tex. Civ. App. 1952).

[134]See Solberg v. Sunburst Oil & Gas Co., 73 Mont. 94, 235 Pac. 761 (1925).

made.[135] And where a lease provides for payment of a rental by depositing it in a bank, and the check is received and the amount credited by the bank to the lessor it makes no difference how the tender is made.[136]

Where a rental falls due on a Sunday it is generally held that the lessee may avoid termination of the lease by payment on the following Monday.[137] It has also been held that where a bank receives a timely rental deposit but fails to credit it to the account of the lessor, such failure is not chargeable to the lessee.[138] Where a lessee in good faith attempts to make a timely payment of rental, but fails to do so on account of non-delivery or miscarriage of the mails, it has been held that, in equity, the lease will not be terminated.[139] However, where the failure to make timely payment of rental is due to the fault or error of the lessee or his employee, the lease was terminated.[140]

In Texas the courts have refused to go as far as have the courts of other states in applying equity to continue leases in force where rental payments were not made in accordance with the terms of the lease. The "determinable fee" principle applies. In a case where there was miscarriage of the mails the court said simply "as a matter of law said rental not having been paid on or before the due date, said lease is forfeited by the force of its own terms."[141] In another case the court said, "Equity does not undertake to dispense with compliance with what is made a condition precedent to the acquisition of a right."[142] In a later Texas case the Supreme Court had before it a situation where the lessor received the lessee's check for rental on the day it was due.[143] The lessee had arranged with the bank for payment of the check when presented, but, through mistake of the bank, payment of the check was refused when it was later presented for payment. The court held that the lease

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[135]Love Petroleum Co. v. Atlantic Producing Co., 169 Miss. 259, 153 So. 389 (1934); Miller v. McGuire, 230 S.W. 421 (Tex. Civ. App. 1921).

[136]See, *e.g.*, LaFayette Gas Co. v. Kelsey, 164 Ind. 563, 74 N.E. 7 (1905); Richmond v. Hog Creek Oil Co., 229 S.W. 563 (Tex. Civ. App. 1921).

[137]See, *e.g.*, Armstrong v. McGough, 157 Ark. 173, 247 S.W. 790 (1923), 29 A.L.R. 236 (1924); Simons v. Adams, 228 S.W. 353 (Tex. Civ. App. 1921).

[138]*E.g.*, Burbridge v. Noc, 69 N.W.2d 286 (N.D. 1955); Hunter v. Gulf Prod. Co., 220 S.W. 163 (Tex. Civ. App. 1920).

[139]*E.g.*, Kays v. Little, 103 Kan. 641, 175 Pac. 149 (1918), 1 A.L.R. 675 (1919); Baker v. Potter, 223 La. 274, 65 So. 2d 598 (1952); Oldfield v. Gypsy Oil Co., 123 Okla. 293, 253 Pac. 298 (1926).

[140]See, *e.g.*, Phillips Petroleum Co. v. Curtis, 85 F. Supp. 399 (E.D. Okla. 1949), *aff'd*, 182 F.2d 122 (10th Cir. 1950); Browning v. Weaver, 158 Kan. 255, 146 P.2d 390 (1944), 5 A.L.R.2d 985 (1945).

[141]Appling v. Morrison, 227 S.W. 708 (Tex. Civ. App. 1921).

[142]Gillespie v. Bobo, 271 Fed. 641, 644 (5th Cir. 1921). See also Empire Gas & Fuel Co. v. Saunders, 22 F.2d 733 (5th Cir. 1927); Texas Co. v. Davis, 113 Tex. 321, 254 S.W. 304 (1923).

[143]Hamilton v. Baker, 147 Tex. 240, 214 S.W.2d 460 (1948).

had not terminated but called particular attention to the rule in Texas that equitable considerations are not applicable unless the case be an exceptional one. However, the court said:

> But it does not become necessary in this case to resort to equitable considerations and reasoning to conclude with certainty that the Baker lease did not terminate. This for the reason that the rentals in dispute were paid by the timely delivery and acceptance of a check which was in fact good, and accordingly the lease was effectively continued in force.[144]

Questions sometimes arise in connection with the correctness of the amount tendered as rental. Surprisingly enough in Texas, where the enforcement of the "determinable fee" principle often works cancellation of a lease where that appears to be a harsh remedy, the courts have taken a more liberal attitude on this question. In the case of *Humble Oil & Refining Co. v. Harrison*[145] a mineral deed covering an interest in the leased premises had been executed and it was ambiguous. This caused the lessee to misconstrue the amount of interest transferred and the rental, as deposited, did not pay the correct amounts to those entitled to receive them. The grantee in the mineral deed was notified of the rental deposit to his credit, but remained silent and did not notify the lessee of the error. It was held that the grantee was estopped to claim that the lease terminated.

However, in a Fifth Circuit case, where the rental payment was incorrect in amount, the court held that "the lease by its very terms ceased to exist."[146] It also held that the lessor was under no duty to notify the lessee that the payment was incorrect. Another Fifth Circuit case, however, held that where the amount of delay rental was slightly less than the correct amount and it was retained by the lessor without objection or complaint, the lessor was estopped to claim termination of the lease.[147]

F. Overriding Royalties

In recent years we have seen a situation develop where producing oil and gas leases become burdened with interests that are called "overriding royalties." The "overriding royalty" is different, of course, from the royalty due the lessor in an oil and gas lease. It is an interest severed out of the lessee's interest, the working interest; it consists of a portion in the lessee's share of the production, and it is not charged with any

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[144] *Id.* at 461.

[145] 146 Tex. 216, 205 S.W.2d 355 (1947).

[146] Empire Gas & Fuel Co. v. Saunders, 22 F.2d 733, 735 (5th Cir. 1927).

[147] Buchanan v. Sinclair Oil & Gas Co., 218 F.2d 436 (5th Cir. 1955); *accord,* Wooley v. Standard Oil Co., 230 F.2d 97 (5th Cir. 1956).

of the cost or expense of development or operation.[148] This is true whether the override is created by reservation, when the original lessee transfers his interest by assignment or sublease, or is created by grant when the lease owner conveys such fractional share to a third person.

Often the overriding royalty is not definitely fixed but may vary in amount, based on the daily production from the lease. In this connection some interesting complications have arisen. In the Texas case of *Butler v. Jenkins Oil Corp.*,[149] where the overriding royalty was provided in the contract as a one-sixteenth override "as long as each well upon said lease *produces* one hundred ninety barrels, or more per day," and one-thirty-second "in the event said well or wells produce less than one hundred ninety barrels per day," it was held that the provision must be taken literally and, where the Railroad Commission of Texas fixed the allowables of the wells at less than 190 barrels per day only a one-thirty-second overriding royalty could be recovered, notwithstanding the fact that the wells were capable of producing 190 barrels per day, or more. Shortly thereafter the *Exum* case[150] was decided by the Fifth Circuit Court of Appeals, where the provision for overriding royalty provided that it should be reduced in the event the total production of oil wells should "decline" to a point below 200 barrels per day; the assignee relied largely on the *Butler* case, but the court drew a distinction between the meaning of the words "produce" and "decline" and held that the overriding royalty should be paid on the basis of the total potential production, notwithstanding the effect of state proration orders restricting production to less than 200 barrels per day. In this case the Federal court observed that the assignee had paid the override on the basis of the higher rate for four years and thereby placed that construction upon the contract.

In another Texas case[151] the override clause provided that the lessor should be entitled to overriding royalty of seven-sixty-fourths, instead of seven-thirty-seconds, on any well which should become "incapable of producing more than 100 barrels of oil per day"; and the court held that this had reference to a "natural deficiency" in production and not to artificial restrictions imposed by state proration and regulations.

In still another Texas case[152] the override was one-sixteenth of seven-eighths while production was 100 barrels or more, and one-thirty-second of seven-eighths while production was less than 100 barrels. Both sides agreed that state allowables or proration orders would govern, but

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[148]See, *e.g.*, Young v. Hill, 247 Ky. 672, 57 S.W.2d 470 (1933); Thornburgh v. Cole, 201 Okla. 609, 207 P.2d 1096 (1949); McDonald v. Follett, 142 Tex. 616, 180 S.W.2d 334 (1944).

[149]128 Tex. 356, 97 S.W.2d 466 (1936).

[150]Exum v. Laub, 87 F.2d 73 (5th Cir. 1936).

[151]Johnston v. Cole, 135 S.W.2d 524 (Tex. Civ. App. 1940).

[152]Kingwood Oil Co. v. Loehr, 200 F.2d 551 (5th Cir. 1952).

the issue was as to how the formula should be applied. The allowable was 120 barrels per day for periods ranging from 15 to 23 days. The assignee claimed that the daily production should be determined by dividing the total produced for the month by thirty; the assignor asserted that the monthly total should be divided by the number of *producing days* allowed by the Commission. Under the former method the production was less than 100 barrels per day; under the latter it was more than 100 barrels per day. The court held that the number of producing days as fixed by the state regulatory body should control in determining the overriding royalty, and plaintiff was permitted to recover on the basis of "100 barrels or more" daily production.

These cases emphasize the fact that in creating an overriding royalty interest, graduated according to production, the party acquiring the interest should be careful to spell out the effect well allowables and proration orders by the state authorities will have on the amount he receives.

Another method of varying the amount of the override is based upon whether the wells are "flowing wells" or "pumping wells." In *Ferguson v. Housh*[153] reformation of a contract was sought which provided for an overriding royalty of three-sixteenths on all "flowing wells" and one-sixteenth on all "pumping wells" on the ground that the provision was ambiguous. The court held that there was no ambiguity and defined a "flowing well" as one that "is caused to produce by its own reservoir pressure," and a "pumping well" as one that requires "the application of some extraneous aids to production."[154]

Where the assignment provided for reduction of overriding royalty "in the event any well drilled on said land quits flowing oil and produces less than 150 barrels per day . . . to be determined by an average of ten days pumping test," it was held that the orders of the Railroad Commission reducing the allowable were not controlling; and, following *Exum v. Laub*, that both cessation of flow and pumping test were conditions precedent to the reduction.[155]

The late Louisiana case of *Esso Standard Oil Company v. Nesbitt*[156] presented a novel situation in determining the amount of overriding royalty due under an assignment of mineral lease. The latter reserved to the assignor three-sixteenths of the oil produced from a well producing over 100 barrels per day and one-eighth where the well produced less than 100 barrels per day. The well was a "dual" completion, that is, it was producing from two sands. The Department of Conservation of Louisiana treats dual completions from one hole as distinct wells and fixes an allowable production from each horizon. Both sands together

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[153]227 S.W.2d 590 (Tex. Civ. App. 1950).

[154]*Id.* at 591.

[155]Midas Oil Co. v. Whitaker, 123 S.W.2d 495 (Tex. Civ. App. 1938).

[156]222 La. 661, 63 So. 2d 417 (1953).

produced more than 100 barrels; separately each produced less than 100 barrels. The operator claimed each sand should be considered a different well in determining the amount of overriding royalty. The owner of the override asserted that it should be considered as one well for this purpose. The court held that it should be considered as production from a single well, requiring the payment to the assignor of a three-sixteenths interest.

It is the general rule that where the owner of a lease assigns that lease to another, and reserves an overriding royalty interest, no fiduciary relationship exists between the assignor and assignee, and the overriding royalty will not apply to renewals and extensions of the lease in the absence of some specific agreement to that effect.[157] In construing the question of whether an overriding royalty in an assignment of a lease will survive the termination of the lease out of which it is created or will inhere in a renewal lease, the court in *Gordon v. Empire Gas & Fuel Co.* said, "There is between assignor and assignee as such no partnership or relation of trust that prevents the assignee from acquiring independent rights to be effective after the expiration of the assigned lease."[158] The same reasoning appears in the Oklahoma case of *Hawkins v. Klein*[159] and other cases.

However, in a recent case by the Supreme Court of Oklahoma some doubt is cast upon the reasoning of those cases, as well as the more general principle as to what is required to create a fiduciary relationship.[160] In the *Rees* case the plaintiffs, Rees and Rodkey, owned three leases, two covering separate portions of the Brouchoud tract and the other covering the Perry tract. The leases each had primary terms of one year only. Plaintiffs assigned their leases to Briscoe on the Brouchoud tract, reserving an overriding royalty. At the same time, Briscoe executed an agreement in writing whereby he obligated himself to commence drilling a well within a certain time and that well was completed as a producer before the leases expired. During the time of the drilling operations on the Brouchoud tract, plaintiffs assigned the lease covering the Perry tract to Briscoe, retaining an overriding royalty. There was no written agreement to drill on the Perry tract as there was on the Brouchoud land. No well was drilled on the Perry tract under the lease assigned to Briscoe and later Briscoe obtained renewals, or new leases, on the Perry tract. The new leases made no mention of plaintiffs' overriding royalty interest. Three years after the leases were

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[157]See, *e.g.*, Gordon v. Empire Gas & Fuel Co., 63 F.2d 487 (5th Cir. 1933); La Laguana Ranch Co. v. Dodge, 17 Cal. 2d 132, 114 P.2d 351 (1941), 135 A.L.R. 546; McDonald v. Follett, 142 Tex. 616, 180 S.W.2d 334 (1944); 3 SUMMERS *op .cit. supra* note 103 at 635.

[158]63 F.2d at 490.

[159]124 Okla. 161, 255 Pac. 570 (1926).

[160]Rees v. Briscoe, 315 P.2d 758 (Okla. 1957).

executed plaintiffs requested Briscoe to give them a recordable instrument recognizing the same overriding interest in the renewal leases that they had owned in the earlier leases. Briscoe refused to recognize the claimed overrides. The trial court heard the evidence based on the plaintiffs' claim that there was an oral agreement to drill on the Perry tract under the former lease, and found against the plaintiffs. The Supreme Court of Oklahoma reversed the trial court, with three Justices dissenting.[161]

The reasoning of the latter opinion is not entirely clear. It doesn't find that there was an oral agreement on the part of Briscoe. The holding that a fiduciary relationship existed between assignor and assignee as to the Perry tract is based on general statements and assumptions. For example, note the following quotation from the majority opinion:

> It is not shown why Rees did not request or require a written agreement as to the Perry tract leases. *This fact is but another proof of the confidence of Rees in Briscoe. . . .*[162]
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> . . . . . .
>
> In the case under consideration Rees received no consideration in cash or otherwise for his lease, except the reserved overriding royalty, which was dependent upon production. It is *unreasonable* to assume that Rees would assign his lease for no present consideration unless he felt that he could depend upon Briscoe to undertake the development of the lease. . . .[163] There is no evidence contrary to that of Rees as to his confidence in Briscoe and his associates. *Had he doubted Briscoe he would no doubt have seen that such provisions were included in his assignments.*[164] (Emphasis added.)

Finally, the court said, "Again, . . . Rees gave up his leases on the Perry land for no consideration whatever and *must have believed that Briscoe would protect his interest. We conclude that the judgment of the trial court is against the clear weight of the evidence.*"[165] (Emphasis added.)

The following quotation from the minority opinion by Justice Williams is of interest:

> The majority opinion . . . does not hold that there was an oral agreement between the parties to drill a well on the Perry tract. . . . As I understand the majority opinion, it holds that plaintiffs had confidence in defendants, and that they had such confidence because defendants had carried out their written contract in the case of the Brouchoud tract, and that since de-

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[161] *Id.* at 764.
[162] *Id.* at 761.
[163] *Id.* at 763.
[164] *Ibid.*
[165] *Id.* at 764.

> fendants had done what they had agreed in writing to do in the case of the Brouchoud tract, they should therefore be required to do that which they had not agreed to do in connection with the Perry tract; that since defendants had agreed to drill the Brouchoud well and had drilled such well in compliance therewith, that plaintiffs had a right to expect defendants to drill a well or wells on the Perry tract without having agreed to do so. I am unable to follow such logic.[166]

G. Implied Covenants of Development

Generally speaking, there are five separate covenants implied in the usual oil and gas lease, unless they are negatived by express covenants therein. Two of them are operational covenants and the other three are development covenants. They are: (1) the implied covenant for diligent and proper operation of wells; (2) the implied covenant to market or utilize the products of the wells; (3) the implied covenant to drill an initial well on the leased premises; (4) the implied covenant to protect the leased premises against drainage by wells on adjoining lands; and, (5) the implied covenant to conduct additional development after paying production is obtained. In order to keep this paper within reasonable bounds, I shall discuss briefly only one of the covenants, the most controversial one, the implied covenant to conduct additional development after paying production is obtained.

The case of *Brewster v. Lanyon Zinc Co.*[167] is regarded as the original and leading authority on the scope and extent of this covenant. The opinion in the *Brewster* case was written in 1905 by Judge Van Devanter, then a judge of the Eighth Circuit Court of Appeals, and later an outstanding Justice of the Supreme Court of the United States. It has been cited as an authority on implied covenants and followed in more than one hundred and fifty cases decided in our leading oil and gas producing states, including decisions by the courts of Texas, Oklahoma, California, Louisiana, Kansas, Illinois, Arkansas, Kentucky, West Virginia, Montana, Wyoming, Michigan and others.

The *Brewster* case arose in Kansas. The facts were that an oil and gas lease gave the lessee two years in which to drill a well on the leased premises, and provided that the time might be enlarged by the payment of an annual rental from the expiration of the second year until the well was drilled; and if no well should be drilled upon "said premises" within five years the lease should be void. A well was drilled during the fifth year which produced gas in paying quantity. No other well was drilled on the lease for a period of fourteen months after the expiration of the five year period, although "many wells had been drilled in the territory adjacent to and surrounding" the leased premises. These wells "pro-

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[166] *Id.* at 766.

[167] 140 F.2d 801 (8th Cir. 1905).

duced oil and gas in paying quantities." There were in this case the issues both of drainage and the drilling of additional wells on the leased premises. Instead of making the judgment of the lessee determinative as to further drilling the court said that in the absence of some stipulation to that effect neither the lessor nor the lessee would be the judge as to extent of diligence to be practiced in developing a lease, but that both are bound by the standard of what is reasonable. The test, therefore, is "reasonable diligence."

1. *"Reasonable Diligence"—Its Meaning*

The *Brewster* case sets forth at least three principles as included in fixing the standard of "reasonable diligence." They are: (1) neither the lessor nor the lessee is the arbiter of the extent to which, or the diligence with which, the operations shall proceed; (2) no obligation rests upon the lessee to carry the operations beyond the point where they will be profitable to him, even if some benefit to the lessor will result from them; (3) the test of diligence required of the lessee is the "prudent operator" test, that is, "Whatever in the circumstances would be reasonably expected of operators of ordinary prudence, having regard to the interests of both lessor and lessee, is what is required." The courts have generally reaffirmed these principles many times.

The first case to enumerate some of the factors which affect the lessee's obligation to conduct further drilling under the "prudent operator" or "reasonable diligence" test was the *Brewster* case. Many later decisions in oil producing states have followed the *Brewster* case, adopting the statement therein naming such factors, and adding others. Among the factors to be considered as affecting "reasonable diligence," and their effect, as enumerated in a number of cases, are: (1) location of lease premises, whether in wildcat territory or producing field; (2) probable quantity of oil and gas capable of being produced from the lease premises as indicated by prior development; (3) the extent of the area normally drained by a well in that field; (4) the character and extent of the subsurface structure and sand in that area; (5) the cost of drilling and operating wells to secure production; (6) the extent and result of operations on adjacent lands; (7) the quantity and quality of the oil and gas reasonably expected to be produced; (8) the prospects for further paying production as revealed by those expert in locating and appraising underground formations; (9) availability of market for the production; (10) transportation facilities for moving the products to market; (11) the effect of conservation regulations and the limitations upon production by state or federal orders; (12) whether, after consideration of all factors, it would appear that the additional well would probably produce sufficient to repay the expense of drilling, equipping and operating such well and also produce a reasonable profit

on the entire outlay. There are many cases enumerating and prescribing the above-mentioned factors as affecting additional development.[168]

2. *Scope of the Covenant—Obligation to Test Deeper Formations*

It is often the case that there is more than one producing formation in a general area. And where there are deeper untested formations underlying a lease that is producing from an upper sand, what is the obligation of the lessee to drill and develop the lower sands? The courts generally have applied the same rule as to deeper drilling that they have announced with reference to further drilling in formations already producing, that is, the "prudent operator" test.[169]

However, Professor C. J. Meyers, Associate Professor of Law at Columbia University, New York City, has proposed a new covenant to apply to deeper drilling on a lease already producing. He would require a lessee to "explore" deeper formations if production from deeper sands is discovered in the general area of the leased premises. His illustrative case was that of a rancher whose lessee has drilled three producing wells on the leased premises and later a deeper producing sand is discovered two miles from the lease. In such case the Professor would impose upon the lessee, where the rancher demanded it, the obligation to "explore" the deeper formations on the rancher's land without considering the prudent operator rule, and whether there is any reasonable expectation of profit from such drilling or not.[170]

This proposed new covenant was expressly repudiated by the Supreme Court of Texas in the late case of *Clifton v. Koontz*.[171] This case attracted widespread interest among members of the Texas Bar, and a number of amicus curiae briefs were filed. The Supreme Court affirmed the judgment of the Court of Civil Appeals. The clear-cut reasoning of the Supreme Court as to the prudent operator rule, the requirement that there must be a reasonable expectation of profit before a lessee is obligated to drill, and the holding that there is no implied covenant to explore as distinguished from the implied covenant to develop, together

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[168]Fischer v. Magnolia Petroleum Co., 156 Kan. 367, 133 P.2d 95; George v. Franklin, 219 Ky. 377, 292 S.W. 1093 (1927); Hutchinson v. Atlas Oil Co., 148 La. 540, 87 So. 265 (1925); Texas Pac. Coal & Oil Co. v. Barker, 117 Tex. 418, 6 S.W.2d 1031 (1928), 60 A.L.R. 936 (1929).

[169]See, *e.g.*, Coyle v. North Am. Oil Consol., 201 La. 99, 9 So. 2d 473 (1942); Texas Consol. Oils v. Vann, 208 Okla. 673, 258 P.2d 679 (1953); Ramsey Petroleum Corp. v. Davis, 184 Okla. 155, 85 P.2d 427 (1939); Texas Pac. Coal & Oil Co. v. Stuard, 269 S.W. 482 (Tex. Civ. App. 1925). See generally MERRILL, COVENANTS IMPLIED IN OIL AND GAS LEASES 174 (2d ed. 1940).

[170]See Meyers, *The Implied Covenant of Further Exploration*, 34 TEXAS L. REV. 553 (1956).

[171]160 Tex. 82, 325 S.W.2d 684 (1959).

with the further fact that the decision was by a unanimous court (one member not sitting) all combine to make this case a landmark decision on implied covenants in the opinion of the members of the Texas Bar generally.

The following statements are taken from the court's opinion. The first deals with the "prudent operator" and "profitability" issue:

> We conclude from all of the above circumstances that the respondents did not violate the implied covenant to reasonably develop the lease by the drilling of additional wells. The petitioners did not discharge the burden which rested upon them to prove, as required, that the lessees failed to measure up to the standard of the prudent operator. While it is true that each separate stratum or horizon would be entitled to separate development, yet it is equally true that the burden rests upon the lessor to prove that the producing stratum required additional wells, or that strata different from that from which production is being obtained, in reasonable probability exist, and that by the drilling of additional wells there would be a reasonable expectation of profit to the lessee. Under such circumstances, the lessee's obligation as to development is measured by the rule of reasonable diligence or what an ordinarily prudent and diligent operator would do, and he is not required to continue in the performance of such implied duties unless there is a reasonable expectation of profit, not only to the lessor, but also to the lessee.[172]

The next declaration sets at rest the proposal to recognize a covenant "to explore" separately from the covenant "to develop." As to this the court said:

> We hold that there is no implied covenant to explore as distinguished from the implied covenant to conduct additional development after production in paying quantities has been obtained. Petitioners argue that the lease involved *expressly* provides for exploration. We agree that, under the terms of the lease, the lessee has the right to explore, but it does not necessarily follow that the lessee is under a duty to explore. To follow petitioners' argument would be to adopt the theory advanced in their "outline of Argument," filed in this Court, that "In an oil and gas lease, the implied covenant reasonably to explore obligates the lessee to drill when a ready, able and willing operator would drill regardless of the certainty of profit. *In support of this theory the petitioners cite the case of Willingham v. Bryson, supra, and Meyers, "The Implied Covenant of Further Exploration," 34 Tex. Law Rev. 553. This theory is untenable and is diametrically opposed to our established "prudent operator," rule where expectation of profit is an essential element.* See Texas Pacific Coal & Oil Co. v. Barker, supra. *We decline to follow the theory advanced that there is an implied covenant to explore as distinguished from the implied*

[172] 325 S.W.2d at 694.

> *covenant to develop. There being no implied covenant to explore, the respondents were under no duty to drill a second or additional well, as found by the trial court.*[173] (Emphasis added.)

Probably the most controversial decision on implied covenants that has been reported in recent years is that of *Sinclair Oil & Gas Co. v. Masterson.*[174] The case, which arose in Texas, was decided by the Court of Appeals for the Fifth Circuit on October 27, 1959, subsequent to the decision in *Clifton v. Koontz,* on June 24, 1959. In the meantime, Professor C. J. Meyers had written his second article for the Texas Law Review in which he cited the findings of fact and conclusions of law by the trial judge in the *Masterson* case as supporting his proposed covenant for further exploration. There were certain findings that appeared to sustain his contention, and others that appeared to support the prudent operator rule. Judgment in the trial court was rendered prior to the decision by the Supreme Court in the *Koontz* case. One finding of the trial court, approved by the Court of Appeals, was as follows:

> It may be said to counsel now, however, that in my judgment a continued recognition of an implied covenant to conduct *exploratory* operations on a lease in search of a mineral covered by the lease, but not yet found, is destined in the law of Texas, and the usual effect of other production to hold the lease in force will not, in the course of time, impede equitable relief where there has been an unreasonable delay in performing the implied covenant.[175]

Also, the appellate court further commented on the lower court's judgment, as follows:

> Based upon its findings and conclusions the court, as stated, ordered Sinclair to drill six *exploratory* wells annually for five years to be spaced as to reflect a good faith effort to make a fair search in different areas for oil production, to be drilled to the horizons the court had found to be those where oil would be found if any should be present.[176] (Emphasis added.)

The Court of Appeals also approved the holding of the trial court that "No burden rests upon the plaintiff to show that the drilling of any or all such exploratory wells would result in profit to the defendant." The decree of the trial court, affirmed by the higher court, further provided that failure of lessee to drill any well could be excused "by surrendering 3,000 acres of its own choosing or paying $50,000.00."

The Court of Appeals, in affirming the trial court's judgment,

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[173] *Id.* at 696.

[174] 271 F.2d 310 (5th Cir. 1959).

[175] Sinclair Oil & Gas Co. v. Masterson, Civil No. 2016, N.D. Tex., Sept. 23, 1958.

[176] 271 F.2d at 315.

made it plain that it was adopting the covenant of "further exploration," notwithstanding the fact that such proposed covenant had been definitely and specifically rejected by the Supreme Court of Texas four months before the Fifth Circuit's decision was rendered. The *Koontz* case was presented and argued to the Court of Appeals, but the latter failed to follow the rules and principles announced by the court of last resort in Texas.

The rule in *Clifton v. Koontz* was reaffirmed, and the reasoning in the *Masterson* case was repudiated in the late case of *Felmont Oil Corporation v. Pan American Petroleum Corporation.*[177] The case was decided by the El Paso Court of Civil Appeals on March 30, 1960, and the Supreme Court refused writ of error, no reversible error, on July 6, 1960.

The facts were that two oil and gas leases were executed in favor of J. W. Grant by T. G. Hendricks and wife on March 27, 1925, covering together 31,360 acres in Winkler County, Texas. One lease covered 10,240 acres and the other 21,120 acres. Each lease was for a primary term of twenty years, and as long as oil or gas, or other named minerals, were produced from the land. A well on one of the leases was completed in 1926, producing in paying quantities and a commercial well was completed on the other lease in 1929. Since those times oil from both leases has been produced in paying quantities. Appellees acquired by assignment a total of "approximately 19,010 acres" covered by the two leases, that is, 5,685 acres of the 10,240-acre lease, and 13,325 acres of the 21,120-acre lease. As to one of the leases, cancellation was sought by the mineral owners of 4,630 acres of the 5,685 acres, owned by appellees and as to the other lease, of which appellees acquired 13,325 acres thereof by assignment, cancellation was sought as to all depths on 3,730 acres, and all depths below 3,200 feet on 900 acres. The opinion recites that "Appellants' suit for cancellation of portions of the two leases is based on the alleged ground that the defendant-lessees and their predecessors in title breached the implied covenant in the leases to explore particular areas of these two leases. . . ."[178] Basing its decision upon the opinion in the *Koontz* case, the court said:

> Assuming as we do that there is no valid distinction between the implied covenant to "explore" and the implied covenant to "develop", the burden rests upon appellants to do more than merely prove that a ready, able and willing operator would drill, regardless of the certainty of profit. Appellants are required to prove:
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> (1) That the lessees failed to measure up to the standards of the prudent operator;

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[177]334 S.W.2d 449 (Tex. Civ. App. 1960).

[178]*Id.* at 451.

> (2) That producing strata or horizons which they contend should have been further explored or drilled, required additional wells;
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> (3) That strata or horizons other than those from which production is being obtained (on which further exploration or drilling is sought), exists in reasonable probability;
>
> (4) That by the drilling of additional wells, there would be a reasonable expectation of profit, not only to the lessor, but also to the lessee. Clifton v. Koontz, Tex. 325 S.W.2d 684; Texas Pacific Coal & Oil Co. v. Barker, 117 Tex. 418, 6 S.W.2d 1031, 60 ALR 936; Brewster v. Lanyon Zinc Co., 8 Cir., 140 F. 801; Rhoads Drilling Co. v. Allred, 123 Tex. 229, 70 S.W.2d 576.
>
> Appellants failed to discharge the burden of proof on these items, no testimony being offered on any of them.[179]

Then, as to "factual situation", relied upon in the *Masterson* case, the court said:

> In the Koontz case (supra), the Supreme Court specifically pointed out that it did not have before it a factual situation where the lease covers several thousand acres, and an effort is being made to hold such vast acreage by showing production from a comparatively small area, nor did it have a situation where an unreasonably long time had elapsed since the last development of the leased premises. In its opinion, the court did not pass upon these questions. Such questions are, however, inescapably before us in the case now under consideration.[180]

As to the duty of the lessee "to explore" the court said, "We hold here, as was held by the Supreme Court in the Koontz case, supra, that there is no implied covenant to explore, as distinguished from the implied covenant to conduct additional development after production in paying quantities has been obtained."[181]

After detailing the development that had been conducted by the lessee-appellees, consisting of the drilling of 80 wells and extensive geophysical work that had been carried on by them at various times on the leased premises and other lands in that vicinity, together with certain farm-out operations, contributions of dry hole money, bottom hole money, and other mediums, all of which the court said was exploratory, the court found that the evidence was sufficient to show that the lessees had discharged their obligations "in the manner of a reasonable, prudent operator, with due regard and consideration to the interest of the lessors as well as the lessees."

As to the *Masterson* case, the court said:

> Appellants have called our attention to the recent case of Sin-

[179] *Id.* at 455.

[180] *Id.* at 456.

[181] *Id.* at 457.

> clair Oil & Gas Co. v. Masterson, 271 F.2d 310, by the Fifth Circuit, which case purports to distinguish and follow the Koontz case. We do not think this case has distinguished the facts of the Koontz case, nor do we believe it follows it. In the Masterson case, the court had before it 31 separate oil and gas leases, each entitled to enforcement with respect to the implied covenants to explore, develop and produce. The court there declined to enforce the implied covenants imposed by each of the leases, presumably on the ground that to do so would impose too heavy a burden on the defendant. Instead, the court treated the 31 separate leases as though they were a single lease covering 90,000 acres. In the absence of an agreement, or the consent of the parties, we know of no rule by which a Texas court would be authorized to take such action. We decline to follow the Masterson case.[182]

Writ of error in this case was denied by the Supreme Court on July 6, 1960.

Another Circuit, in deciding similar issues, presents legal reasoning quite different from that found in the *Masterson* case. The *Masterson* case was decided by the Fifth Circuit on October 27, 1959, and six days later, on November 2, 1959, the Tenth Circuit rendered an opinion on facts somewhat similar to those in the *Masterson* case.[183]

In the *Blythe* case the lease was executed in 1944, and covered 920 acres. Out of this lease a tract of 280 acres was assigned to Sohio. Production of both oil and gas was obtained on the 920-acre tract. Fifty-one wells were drilled to exploit the shallow sands, and of this number 24 were productive of either oil or gas and the remaining 27 were dry holes. As to the 280 acres assigned to Sohio, only one producing well was drilled by Sohio, but assignees of Sohio drilled and completed 10 producing wells under farmout agreements. This suit was instituted *thirteen years* after the original lease was delivered, and sought to cancel the lease on an 80-acre tract included in Sohio's assignment on which no wells at all had been drilled.

The case presented no issue as to the drilling of shallow wells on the 80-acre tract. It was admitted that there was no reasonable expectation of obtaining production from the shallow sands on this 80 acres. The issue arose as to Sohio's failure for *thirteen years* to develop the deeper sands, centered mainly in the Simpson formation, found at depths of anywhere from 5,000 feet to 12,000 feet below the surface. The evidence showed that it would cost Sohio $238,000 to drill a well to these lower horizons. Further, it was shown that, although there had been a delay of thirteen years in developing the 80-acre tract, interest in the possibilities of *deep* production was not "intensified" until the last three years of that period. The court said:

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[182]*Id.* at 458.

[183]See Blythe v. Sohio Petroleum Co., 271 F.2d 861 (10th Cir. 1959).

> Equity would not require Sohio to expend $238,000 to explore these great depths during a period of time (10 years or more) when there was no *general interest* therein or belief that production of oil or gas might be found therein. The question then is, did Sohio act in bad faith in disregard of lessor's rights by not undertaking this *expensive* drilling operation during the three or four years that opinion and knowledge concerning these deep formations was crystallizing? We think not. (Emphasis added.)

The court then said that Sohio had exercised reasonable diligence (1) in seeking permission to do seismic work on the Blythe lease, which was refused; (2) in making "arrangements" with other operators for the drilling "in the near future" of a well to a projected depth of 12,500 feet on a unitized tract in the section adjoining that containing Sohio's acreage; and (3) in producing "other evidence showing that Sohio was alert to the possibilities of future production from this strata."

The court definitely stated that Sohio's obligation was subject to the "prudent operator" rule, referring to the case of *Trust Company of Chicago v. Samedan Oil Corporation*,[185] and saying that in that case, "Chief Judge Murrah reviewed and analyzed in detail the leading Oklahoma cases dealing with the prudent operator rule, as applied in Oklahoma." Implicit throughout the decision is the court's expressed purpose (1) of following the Oklahoma decisions, (2) applying the prudent operator rule, and (3) not requiring Sohio to undertake "expensive" drilling unless a prudent operator would conduct such development.

An examination of the many decisions involving implied covenants of development or additional drilling reveals the difficulty courts have in applying fixed principles to varying fact situations. No two cases present the same facts. The standard of "reasonableness" is applied to both the lessor's demand and the lessee's duty, and the reasonableness depends upon the facts and circumstances of each case, where there is enough evidence to bring the case within the purview of the covenant's requirements. When that occurs it is for a court of equity to exercise its discretion in applying the three fundamental rules: (1) Neither the lessor nor the lessee is the arbiter of the extent to which, or the diligence with which, the operations shall proceed; (2) no obligation rests upon the lessee to carry the operations beyond the point where they will be profitable to him, even if some benefit to the lessor will result from them; and (3) the test of diligence required of the lessee is the "prudent operator" test, that is, "whatever in the circumstances would be reasonably expected of operators of ordinary prudence, having regard to the interests of both lessor and lessee, is what is required."

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[184] *Id.* at 864.

[185] 192 F.2d 282 (10th Cir. 1951).

PROCEDURAL REFORM IN MISSISSIPPI

PART I

L. G. Fant, Jr.*

I. The Great Tradition

A. Early Movements

Historically, reform of procedural law has been a slow process. The first tangible reform of common law pleading in England, the "Hilary Rules" of 1834, was effected sixty-eight years after the movement for reform was set in motion.[1] The Act of 1834 had the effect of limiting the use of the plea of general issue.[2]

Code pleading had its beginning in this country with the New York Code of 1848.[3] As will be shown below, a century passed before any significant change was effected in the law of pleading of Mississippi. In the federal courts, the movement for procedural reform was commenced in 1912.[4] The statute which led to the adoption of the Federal Rules of Civil Procedure was not enacted until 1934.[5] It is not the purpose of this paper to inquire into the reason why procedural law tends to be static, so much as to suggest that in 1962 further progress in Mississippi may be at hand.

B. Early Developments

Common law pleading was, of course, a creature of the courts whose main object was to arrive at an issue of fact.[6] The New York Code of 1848 was the result of work by a commission created by the legislature.[7] The first report of the New York commissioners recommended that the complaint should contain "a statement of the facts constituting the cause of action in ordinary and concise language without repetition, and in such a manner as to enable a person of common understanding to know what is intended."[8]

The effort to reform pleading in Mississippi has been long and largely unsuccessful.[9] Traditions of common law pleading seem to have

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Part II will appear in December 1963.

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[1]See Clark, Code Pleading 18 (2d ed. 1947) [hereinafter cited as Clark].

[2]*Ibid.*

[3]*Id.* at 19.

[4]*Id.* at 34.

[5]*Id.* at 35.

[6]*Id.* at 12.

[7]*Id.* at 22.

[8]New York Commissioners on Practice and Pleadings, First Report on the Code of Procedure § 120 (1948).

[9]See Griffith, *The New Mississippi Civil Practice Act—Its Background and Effect,* 20 Miss. L. J. 1 (1948).

been maintained with minor statutory changes.[10] Wide movement for reform of a century ago, however, had some effect in Mississippi.[11] The Circuit Court Act of 1822 had already provided that in personal actions if the declaration set forth sufficient substance for the court to proceed upon the merits, the suit should not be abated for want of form.[12] In the next published code the following provision is found: "The declaration shall contain a statement of the facts constituting the cause of action, in ordinary and concise language, without repetition, and if it contains sufficient matter of substance for the court to proceed upon the merits of the cause, it shall be sufficient."[13]

C. Effect of Early Developments

Although the language of the Code of 1857 was said to have abolished all forms of action,[14] vestiges of the formulary system seem to remain. In *Town of Hazelhurst v. Cumberland Tel. & Tel. Co.* action was brought by the town against the telephone company in two counts.[15] The first count alleged the contract with the town and the second count demanded the value of the use of the streets. A general demurrer was sustained and plaintiff appealed. In the Mississippi report the argument advanced for the appellee was the quotation from Chitty: "[I]t is a general rule that actions in form *ex contractu* cannot be joined with those in form *ex delicto*."[16] In a brief opinion the judgment was affirmed, the Supreme Court citing Chitty[17] with the remark, "Our code does not change this." This decision was cited with approval as late as 1940.[18] In *Miller v. Wesson,* however, the court permitted the joinder of a count for statutory penalty for trees, a count for the value of trees cut and a count for the money received from their sale, saying, "Each count is as distinct as if it was in a separate declaration, and must be tried by itself, except as it may contain a reference to another in expressed terms."[19] On this point, the decision has been distinguished as not being authority for the proposition that plaintiff may recover both the statutory penalty and the actual value of the trees.[20] It therefore seems difficult to reconcile the *Miller* case with the *Hazelhurst* case.

The authorities need not be exhaustive to illustrate complexity.

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[10] *Ibid.*

[11] See *ibid.*

[12] Miss. Laws 1822, § 89, at 50.

[13] Miss. Rev. Code ch. 61, art. 78 (1857).

[14] Evans v. Miller, 50 Miss. 120 (1880).

[15] 83 Miss. 303, 35 So. 951 (1903).

[16] 1 CHITTY, PLEADING *228.

[17] *Id.* at *223.

[18] Gulf M. & N.R.R. v. Madden, 190 Miss. 374, 390, 200 So. 119, 124 (1941).

[19] Miller v. Wesson, 58 Miss. 831 (1881).

[20] Roell v. Shields, 124 Miss. 226, 86 So. 763 (1920).

In *Illinois Cent. R. R. v. Abrams,* Abrams sued the railroad for personal injuries and recovered a judgment.[21] So far as the report, which includes the briefs, shows, there was no demurrer or other attack on the declaration. Appellant argued that there was no liability. The Supreme Court, in an opinion by Chief Justice Whitfield, found that the declaration was peculiar in that, while chiefly framed on liability for failure to furnish plaintiff a safe place in which to work, it also contained scattered clauses which, the court said, "seem to be some sort of an attempt in rather an obscure fashion to hold the defendant liable under Section 193 of the Constitution of 1890." This, the court condemned, saying: "Reversible error has been committed plainly and flagrantly, in putting, in a declaration with but one count, two antagonistic causes of action, and in respect also of the course pursued in giving instructions as to both these antagonistic causes of action under this peculiar declaration."[22]

The *Abrams* case has been cited,[23] distinguished[24] and greatly limited in effect.[25]

Passing the question of the lack of demurrer or motion in the *Abrams* case, however, decisions make it clear that principles of common law pleading have been preserved. For example, in 1934 in *Aetna Ins. Co. v. Commander* the court said:

> The common law rule forbidding duplicity in pleading is one of convenience only, and its purpose is to prevent the opposite party from being prejudiced or embarrassed in the trial of the cause. That purpose is taken care of by Section 554, Code of 1930 . . . under which if the duplicity in a pleading is of such character "as to prejudice, embarrass, or delay a fair trial of the action, the court on the application of the opposite party, shall cause the same to be made definite and certain or may strike the same from the files."[26]

In the same decision the court said: "One of the common law rules is that 'whatever is alleged in a pleading must be stated with certainty,' a violation of which was subject to a special demurrer. This rule was brought forward, with its scope somewhat restricted, in the statute which now appears as Section 521, Code 1930."[27]

Southeastern Express Co. v. Namie was decided in 1938.[28] In this case, Namie sued the Express Company for damages alleging that cer-

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[21] 84 Miss. 456, 36 So. 542 (1904).
[22] *Id.* at 464, 36 So. at 543.
[23] Jackson v. Cook, 214 Miss. 201, 58 So. 2d 498 (1952).
[24] Aetna Ins. Co. v. Commander, 169 Miss. 847, 153 So. 877 (1934).
[25] *Id.* at 854, 153 So. at 879.
[26] *Id.* at 855, 153 So. at 880.
[27] *Id.* at 853, 153 So. at 879.
[28] 182 Miss. 447, 181 So. 515 (1938).

tain pelts were negligently damaged by defendant. The declaration included allegations that plaintiff delivered the pelts in good condition to defendant for carriage. There was a verdict and judgment for plaintiff. On appeal, defendant argued that there was no evidence of negligence. The court, speaking through Justice Griffith, said:

> On the trial appellee failed to prove the specific negligence charged and now appellant insists, as its chief contention, that it was entitled to the peremptory charge requested by it, the argument by appellant being, in effect, that appellee having gaged his legal battle on the issue of negligence as the gist of his cause of action and having failed to sustain that issue, appellant is entitled to the award of a verdict. This contention, upon first approach, is liable to be considered plausible, and we think it merits more than a cursory discussion.
>
> The rule is fundamental, of course, that when a plaintiff has alleged and proved the facts essential to a recovery, he is entitled to judgment. It follows that it is unnecessary to allege or prove more, and that if more than enough be alleged, the unnecessary allegations will be treated as surplusage. It follows further that an unsuccessful attempt to prove the surplus allegations will not defeat the plaintiff; for having alleged and proved enough he is not entitled to lose his case merely because he alleged but failed to prove more than enough. Under our statutes abolishing forms of action and requiring that merits only shall be considered, Section 521, Code 1930, the rule goes so far that a recovery may be had in contract, if the allegations and proof support such a right, although the declaration sounded in tort.[29]

Anyone attempting to reconcile this decision with the *Hazelhurst* case encounters difficulties which are apparent.

The *Hazelhurst* decision appears to rest on the common law concept of the nature of causes of action.[30] The author of the *Namie* opinion explained it as resting on a principle governing appeals, saying:

> The rule that a party on appeal shall be held to the theory upon which he presented his case in the trial court goes no further than the reason which gives it life. The reason is that had the case been presented to the trial court upon a different theory, the opposite party might have met and overturned that theory by adequate proof. But when all the facts necessary to a recovery by a plaintiff . . . are admitted by the defendant . . . all that remains is to apply the law.[31]

The vigor of common law concepts is reflected in a recent decision.[32] In a default judgment in an action of replevin, the portion of

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[29]*Id.* at 459, 181 So. at 516.

[30]See SHIPMAN, COMMON-LAW PLEADING § 80 (3d ed. 1923).

[31]Seward v. First Nat'l Bank, 193 Miss. 656, 669, 8 So. 2d 236, 240 (1942) (dissenting opinion).

[32]Road Material & Equip. Co. v. McGowan, 229 Miss. 611, 91 So. 2d 554 (1956).

the judgment awarding money to the plaintiff as well as possession of the personal property was held to be void, so that it could be set aside by the court at a later term. In this opinion, an earlier decision[33] was distinguished.

In keeping with its common law traditions of pleading, Mississippi has a statute of Jeofails which reads in part: "A judgment shall not be stayed or reversed after verdict for any defect in the writ, or for a variance in the writ from the declaration or other proceedings; or for any mispleading, insufficient pleading. . . ."[34] In applying this statute, the court has long distinguished declarations which do not state a cause of action from those in which it is said a cause of action is defectively stated. The statute is held not to apply to the first class[35] but only to the second.[36]

In *Wilson v. Terry*,[37] after judgment by default and judgment on writ of inquiry, defendant appealed to the Supreme Court. The action was for personal injuries and the declaration stated that plaintiff "on account of the negligence of the driver" suffered her injuries. The Supreme Court made the distinction, held that in this case the declaration did not state a cause of action and reversed the judgment. In its opinion, the court discussed allegations that would have been necessary to support the charge of negligence, saying:

> It seems to be generally recognized that to maintain an action for negligence, the declaration must charge that the defendant was under a duty to use care; that he failed to do so; and that the plaintiff was injured as the proximate result thereof.
>
> . . . . Wilson [defendant] was under no obligation to hunt up information that might perhaps make out a case against him. He was bound to take notice only of the allegations, if any, against him in the original and amended declarations. If he did that, he could not have found the charge that he was under a duty to use care toward the plaintiff or that he failed to do so or that she was injured as a proximate result thereof.[38]

Conceding that Mississippi has never been known as a "code pleading state," even a brief review of the decisions is believed to show that at this late date the subtle distinctions and technical rules of "the science of pleading" are well preserved. This review also demonstrates that, though the legislature from time to time has passed or amended a statute on pleading, the controlling rules have been formed by the decisions of the Supreme Court. Referring to the time of Henry VI, it

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[33]Frierson v. Mississippi Road Supply Co., 221 Miss. 804, 75 So. 2d 70 (1954).

[34]MISS. CODE ANN. § 1544 (1956).

[35]*E.g.*, Wilson v. Terry, 218 Miss. 411, 67 So. 2d 387 (1953).

[36]*E.g.*, Oliver Bus Lines, Inc. v. Smith, 164 So. 43 (Miss. 1935).

[37]218 Miss. 411, 67 So. 2d 387 (1953).

[38]*Id.* at 416, 67 So. 2d at 388.

was said, "The calamity has been that after other branches of knowledge took a more liberal turn, the minutiae of pleading continued to be respected with a sort of religious deference."[39]

II. The Great Divorce

A. Goals of Reform

It is not intended to suggest that the rules of civil procedure can be made simple. The arduous functions required of pleading have contributed to the complexity of the rules. At common law, the chief function of the pleadings was framing of issue.[40] While the common law pleading stated some facts, the emphasis on development of an issue resulted in formal, general statements of fact.[41]

At the beginning of the reforms in the 19th century, formal statement of fact was considered the great defect and pleading "in ordinary and concise language, without repetition" was the goal sought by the statutes.[42] As reflected by the statutes and decisions above, pleading of "facts" is the goal in Mississippi. Pleadings are considered, therefore, to have three functions: (1) the giving of notice, (2) the forming of issue, and (3) the revelation of facts.[43]

B. Analysis of Results

The usefulness of pleadings as a source of information is extremely doubtful. The code commissioners of New York recognized the difficulty in 1848: "There has been a constant struggle of the pleaders and the courts to evade their own rules. They made them and they defend them as the means of eliciting the precise point in dispute, and they seek every means in their power to conceal it under the most general allegations."[44]

There are other compelling reasons why the pleadings may be generally said to fail to reveal the facts. One such reason is the difficulty in defining "facts."[45] They must be distinguished from the evidence and from conclusions of law. An allegation that a passenger was "wrongfully ejected from a train by a conductor, in the presence of many passengers, with great indignity and wrong and hardship" is a conclusion, so that the court took the allegation on demurrer as being that plaintiff was properly and politely ejected.[46]

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[39]Shipman, *op. cit. supra* note 30, at 6 n.11.

[40]*Id.* at 298.

[41]See Clark § 38.

[42]*Id.* at 226.

[43]*Ibid.*

[44]*Id.* at 226 n.53.

[45]*Id.* at 226.

[46]Mitchell v. Southern Ry., 77 Miss. 917, 27 So. 834 (1900).

Another great obstacle to performing the function of fact-revelation in pleadings is that the pleader himself does not know the facts of his case until he has heard the evidence. Obviously, the facts of a case have importance other than in preparation for trial. The facts will govern the issues, and the establishment of these facts will determine the legal rights of the litigants.

In Mississippi procedural law, however, with certain exceptions, the lawyer is remitted to the formal writings of his adversary for discovery of the facts. If a party satisfies the court by affidavit of his need, the court may order a bill of particulars.[47] This is a time consuming process. If he is willing to take the risk of the sworn answer he may be able to maintain a bill of discovery in chancery.[48] This ancient bill of chancery originated in the time when a party in interest was not a competent witness.[49] To have the expense and delay of a suit in chancery, fraught with the grave dangers inherent in the sworn answer, may be as unsatisfactory a means of attempting to discover a fact as has ever been devised.[50]

Another alternative, of course, is to take depositions.[51] The limitations on the taking of depositions and the procedure for taking those of witnesses within the state, however, are substantially the same as are found in the Code of 1857.[52]

Further, after notice to the adversary, an order can be obtained from the court for an inspection and copy of any books, papers or documents, accounts, letters, photographs, objects or tangible things containing evidence relating to the merits of the action.[53] With minor changes this statute is in the Code of 1857, also.[54]

The next source of information is a comparative novelty. It is first found in the Code of 1880.[55] One may file interrogatories directed to the party of the suit who resides out of the state.[56] This statute has been amended in a manner mentioned below.

These are the tools of discovery presently available to the Mississippi lawyer in the courts of this state. With a single exception, they were available to his great-grandfather.[57] The intention is not to suggest that antiquity is of itself a flaw. However, it is intended to suggest that

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[47]MISS. CODE ANN. § 1499 (1956).

[48]See GRIFFITH, MISSISSIPPI CHANCERY PRACTICE §§ 427-32 (2d ed. 1950).

[49]*Id.* § 427.

[50]See Fant v. Fant, 173 Miss. 472, 162 So. 159 (1935), which involved the predecessor to MISS. CODE ANN. § 1294 (1956). See generally Annot. 1 A.L.R. 105 (1919).

[51]MISS. CODE ANN. §§ 1699-1709 (1956).

[52]Miss. Rev. Code ch. 61, art. 209 (1857).

[53]MISS. CODE ANN. § 1659 (1956).

[54]Miss. Rev. Code ch. 61, art. 236 (1857).

[55]Miss. Rev. Code § 1943 (1880), which is now MISS. CODE ANN. § 1712 (1956).

[56]*Ibid.*

[57]MISS. CODE ANN. § 1712 (1956).

in so important a matter as discovery of facts the lawyers of Mississippi and, even moreso their clients, deserve the best procedural laws procurable. These observations obviously are prefatory to a mention of the Federal Rules of Civil Procedure.

C. Federal Rules of Civil Procedure

One of the most important procedural changes made by the Federal Rules is the separation of revelation of facts from pleadings.[58] By the discovery process[59] pleadings are relieved of their top-heavy load of both forming issues and disclosing facts.[60] In federal courts the lawyer himself can (1) determine the true issue, (2) obtain evidence for use at the trial, and (3) secure information as to the existence of evidence that may be used at the trial.[61] In addition, he may learn how and from whom this evidence may be procured.[62] Common examples are the existence and location of documents and the names and addresses of persons having knowledge.

This innovation has had a catalytic effect on pleading. No longer is it necessary that the "facts" be pleaded, or that the formal pleadings devised by the lawyer determine the issues. Pleadings become simpler; they need only set forth a claim.[63] So revolutionary a change as that effected by the "new rules" of federal procedure produced shock.[64] However, Mississippi lawyers have practiced in federal courts under these rules for nearly twenty-five years. It may be doubted if any one of them would now advocate a return to the former federal practice.

III. Recent Developments

A. Legislation Since 1948

The above discussion in this article has been intended to serve as a prologue for consideration of recent changes in Mississippi procedural law. While the changes are slight, it is thought that the fact of their occurrence may be significant.

In point of time, the first change occurred in 1948. Under an impetus not necessary to be examined here, the legislature abolished the plea of general issue.[65] There was substituted the familiar requirement of an answer in chancery: "The defendant shall answer fully all the al-

[58]See 2A Barron & Holtzoff, Federal Practice and Procedure § 641 (rev. ed. 1961).

[59]Fed. R. Civ. P. 26-37.

[60]See 2A Barron & Holtzoff, *op. cit. supra* note 58, § 641.

[61]*Ibid.*

[62]*Ibid.*

[63]Fed. R. Civ. P. 8(a).

[64]See Clark 63.

[65]Miss. Laws 1948, ch. 230, which is Miss. Code Ann. § 1475.5 (1956).

legations of the declaration without being specially interrogated."[66] This change is believed to have two-fold significance: (1) The first reform of common law pleading in England, the "Hilary Rules," sometimes called the "new rules," had as their main accomplishment the limitation on the plea of general issue.[67] It is significant that one hundred fourteen years later the legislature of Mississippi took a similar step. (2) In the light of considerations advanced, however, it may have seemed but a step down the dark avenue of fact pleading. To require the defendant to answer fully all the allegations of the declaration, without being specially interrogated, is but a device of discovery known for centuries to the chancery court.[68] This would seem to rest upon the doubtful premise of truthfulness, i.e., discovery of facts may be obtained in pleading.[69] Any lawyer familiar with bills of complaint and answers in the chancery court must agree that the "full" answer formerly required in that forum is not enlightening on the facts.

The next change occurred in 1950. The statute to which reference was made above[70] was quietly amended by adding one sentence: "A denial by the defendant by reference to a designated paragraph shall be deemed a sufficient denial of the allegations of that paragraph except such as are specifically admitted."[71] The purpose of this amendment, that is to say, the design of the person who drew the bill is not known. At first glance, it may have seemed a sly return to the use of the general issue. However, this was not the result. It is submitted that the consequence has been a continuation of fact pleading, with the mere convenience of denying a part or all of a paragraph without the laborious use of disjunctives so common in the ordinary answer formerly required in chancery. This form of pleading is familiar in the federal court.[72]

Without controversy the legislature in 1962, for the first time in the history of the state, amended the law of pleading in chancery to allow a similar denial.[73] It may be said, therefore, that the dubious effort of a century to require the pleader to give the true facts of the case has now been abandoned. The defendant pleads in both the circuit and chancery courts in much the same manner in which he pleads in the federal court under the "new rules" of federal procedure.

The third change occurred in 1956. The statute, in effect since 1880,[74] providing written interrogatories to a non-resident party was,

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[66]Miss. Laws 1948, ch. 230, § 2.

[67]CLARK 18.

[68]GRIFFITH, MISSISSIPPI CHANCERY PRACTICE § 350 (2d ed. 1950).

[69]See *id.* § 20 (d).

[70]MISS. CODE ANN. § 1475.5 (1956).

[71]Miss. Laws 1950, ch. 356, § 2.

[72]FED. R. CIV. P. 8 (d).

[73]Miss. Laws 1962, H.B. 584.

[74]MISS. CODE ANN. § 1712 (1956), which was Miss. Rev. Code § 1943 (1880).

again, quietly amended to provide such written interrogatories to a party whether resident or non-resident of the state.[75]

B. Significance of Recent Legislation

Here, then, are changes made in the procedural rules of the courts of Mississippi in a period of approximately eight years. They are the first changes effected of any particular significance since the adoption of the Code of 1857. It may be that their significance has been exaggerated. However, when a body of law has remained static for one hundred years, it is believed that a change of any kind has some significance. In this instance, moreover, the changes seem to reflect the experience of Mississippi lawyers with the Federal Rules of Civil Procedure.

Since 1956 we have had, however limited, a form of discovery.[76] It is true that it is limited in its scope and is cumbersome in its nature. It is limited to the production of evidence and can be used only to the opposite party. It is cumbersome in nature because it requires written interrogatories. Eliciting information of value by written interrogatories is an arduous task. Nevertheless, whatever its limitations, it is a form of discovery. With the introduction of this form of discovery has come a relaxation in the requirements of fact pleading on the part of the defendant.

Future changes which may now be at hand will not be so great a departure from the existing law of procedure as were changes in the past.

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[75]Miss. Laws 1956, ch. 237.

[76]Miss. Code Ann. § 1712 (1956).

RECENT INTERESTING DECISIONS IN NEGLIGENCE AND INSURANCE LAW

*Ernest W. Graves**

I. Introduction

A quick glance at recent issues of the Southern Reporter is sufficient to indicate that the Mississippi Supreme Court is under a veritable deluge of negligence cases. All of the work of the court for the past year in this field is, to some extent, interesting; however, for the purposes of this article, there must be some arbitrary picking and choosing. Frustrating problems in selection arise where choice is almost unlimited. What follows is no more than a catalogue, with the bare minimum of editorial comment, of some helpful and enlightening decisions. The best purpose it can serve is to indicate trends in the handling of negligence and insurance issues. The only other purpose is to note some of the specific rulings in the field which will likely be of lasting importance.

II. Parties Defendant

A. Husband - Wife

A case which has wound its tortuous and technical way through the courts since 1952 received its death blow this year in *Ensminger v. Campbell.*[1] The plaintiff had originally brought suit against her husband for injuries sustained in an automobile accident. A demurrer to the original bill in Chancery was sustained on the ground that a wife cannot maintain an action against her husband in tort. Subsequently a divorce was granted, and then the husband died. The ex-wife reinstituted the suit against the administrator. The court held that there was no cause of action at the time of the accident, and that none arose because of the subsequent divorce.

B. Municipal Corporations, Counties

The statutory action for injuries to children while passengers on a school bus[2] has received further interpretation in *Durr v. Alfred Jacobshagen Co.*[3] There, the minor plaintiff brought suit for injuries sustained in a collision between a truck and the school bus on which she was riding; the drivers of the two vehicles, the trucking company, and

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Mr. Graves was assisted in his research by Mr. John Adams, a student at the University of Virginia School of Law.

[1]134 So. 2d 728 (Miss. 1961).

[2]Miss. Code Ann. § 6336-19 (Supp. 1960).

[3]139 So. 2d 852 (Miss. 1962).

the county were named as parties defendant. The declaration asked for damages in the amount of $50,510.00, although the statutory limit on a county's liability is $5,000.00.[4] The court held that the trial court erred in sustaining the county's plea in bar; the mere fact that the declaration asked for damages in excess of what the county was required to pay was found to be no defense to the suit against the county where there were other defendants. The case leaves unanswered the question of how the jury, if finding for the plaintiff, would write its verdict.

Hawkins v. City of Natchez[5] reaffirmed that a municipality can be liable for damages caused by negligence in the operation of its drains and sewers, but the case resulted in a judgment for the defendant city. The plaintiff brought suit for the death of her young child who fell into an open, water-filled ditch and was swept into a culvert and drowned. The sidewalk along the ditch was found to be reasonably safe for use by an *adult* using reasonable care; the fact that the deceased was a child was impliedly found to be irrelevant.

C. Carriers

The exceptional duty owed by carriers to their passengers is the basis of the decision in *Continental Southern Lines, Inc. v. Robertson.*[6] The case stands for the proposition that when a passenger is injured while in transit, even if by his own negligence, the carrier must procure immediate medical attention or stand liable for any aggravation of the injuries caused by its negligence. The plaintiff here had wrenched her knee while sitting in her seat. Although repeatedly asking for medical attention, she was treated only by two agents of the carrier, and no doctor was seen until the journey was completed. The carrier was held liable for not procuring medical attention to alleviate the pain and suffering of its helpless passenger.

D. Respondeat Superior

A situation which is likely to arise more frequently, as civic pride and community spirit take more tangible forms, is presented in *West Bros., Inc. v. Herrington.*[7] Various civic groups in Hattiesburg, along with the University of Southern Mississippi, were planning a civic parade in connection with the University's Golden Anniversary and first home football game. West Brothers furnished its truck for the parade, but it was driven by an unpaid volunteer who had no connection with the owner. Reversing and entering judgment for the defendant, the

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[4]Miss. Code Ann. § 6336-19 (Supp. 1960).
[5]133 So. 2d 610 (Miss. 1961).
[6]241 Miss. 796, 133 So. 2d 543 (1961).
[7]139 So. 2d 842 (Miss. 1962).

court rejected the doctrine of respondeat superior and decided that the volunteer driver was certainly not engaged in the business of West Brothers at the time of the accident. To be especially noted is the fact that the truck carried the name of the owner corporation painted on its side so that the lending of the truck might be assumed to be, to some extent, an advertising venture aimed at promoting good will. But the court found that such minimal factor was not enough to establish vicarious liability. Substantial out-of-state authority is cited in favor of the holding.

E. Third-Party Tort-Feasors under the Workmen's Compensation Law

Respect for or disregard of the corporate entity has become a crucial point in the area where tort liability and workmen's compensation merge. Intriguing indeed is the case of *Index Drilling Co. v. Williams*,[8] and for reasons other than the fact that a Jones County jury awarded $63,500.00 for the loss of a big toe and a second toe, suffered while unloading a truck. The plaintiff had received workmen's compensation from one of five related corporations, but he was successful in bringing a third party action against another of the five. The five corporations were virtually indistinguishable in certain areas, and the brief summary of the evidence given in the opinion indicates that at the time in question the plaintiff was receiving orders from the agents of at least two of the corporations. But the borrowed servant doctrine was held to have no application, and immunity from tort liability was limited to the precise employer and carrier, and did not extend to any of the related corporations. Liability was affirmed, but a new trial was ordered on the question of damages. There was strong evidence that the jury had reached a quotient verdict, but it was insufficient to prove that there was a prior agreement among the jurors to accept the quotient obtained as their verdict. The court pointed out that jurors cannot impeach a verdict duly rendered by them and that their affidavits introduced for such purposes will be disregarded.

III. Proximate Cause

An occasional case will serve to remind the legal profession that the events of some tragic occurrences are so obscure as to leave liability outside the realm of judicial determination. One such case, *Denman v. Denman*,[9] was a suit by a six-year-old auto passenger against the estate of her grandmother. A tragic head-on collision occurred at dusk with rain and fog involved; the grandmother, the driver of the other car, and

[8] 137 So. 2d 525 (Miss. 1962).
[9] 134 So. 2d 457 (Miss. 1961).

a passenger were all killed, leaving no eye witnesses. Circumstantial evidence was insufficient to establish the grandmother's negligence. The doctrine of res ipsa loquitur was not applicable. Wreckage was scattered, and very little could be told from a survey of the accident scene. Although recognizing that negligence may be established by circumstantial evidence provided the circumstances are such as to take the case out of the realm of conjecture and place it in the field of legitimate inference, the court found that a directed verdict had been properly given the defendant. The plaintiff's theory of the case was subject to speculation and conjecture. The court reiterated that verdicts must rest upon reasonable probabilities. The companion case, in which the same plaintiff brought suit against the estate of the driver of the other automobile, likewise resulted in a finding of no liability.[10]

The problem of tracing obscure connections of cause and effect has resulted in two cases involving injury to animals. *Bridges v. Texaco, Inc.*[11] arose out of two severe geophysical explosions set off very close to the plaintiff's chicken houses. The noise and force of the explosions, which were so powerful as to knock a chair over on a nearby porch, sent the chickens into a turmoil. About two days afterward, egg production began to drop sharply and never regained its normal level. Expert witnesses for the plaintiff testified that chickens raised in enclosures were easily subject to fright and that in their opinion the explosions so frightened the chickens that they went into partial moult. Prescribed medications did not help the situation and the chickens were eventually sold for meat. The Supreme Court held that the plaintiff had made out a prima facie case, and that the directed verdict for the defendant was improper.

In *Brunt v. Chicago Mill & Lumber Co.*,[12] the plaintiff was the owner of a herd of cattle pastured along a levee. The evidence tended to show that a small aircraft under the direction of an agent of the defendant took off from the levee and passed very low over the cattle, and that the cattle were thereby stampeded through a fence and lost near the river. The court held that the negligence of the defendant was a question for the trier of fact, and reinstated the judgment of the county court which had been reversed by the chancellor. It was held that the ordinary rules of negligence and proximate cause relate to the operation of airplanes.

IV. Products Liability

A time-honored principle among appellate courts, that they will not rule upon highly controversial and difficult questions of law when

[10]Denman v. Spain, 135 So. 2d 195 (Miss. 1961).

[11]136 So. 2d 595 (Miss. 1962).

[12]139 So. 2d 380 (Miss. 1962).

a case may be decided upon a simpler ground, has been recently applied by the Supreme Court in the field of products liability. In *Harrist v. Spencer-Harris Tool Co.*[13] the court declined to rule upon, and therefore sustained, the requirement of privity of contract in products liability suits. The plaintiff, the employee of a drilling company (named a defendant for purpose of garnishment process), brought suit against the manufacturer and vendor of a drilling rig. The bill alleged that the plaintiff fell down the steps of the rig, and that his fall was caused by the inherently dangerous nature of the steps which slanted downward. In arguing that the chancellor had improperly sustained the defendants' demurrer, the appellant relied upon a dictum in an earlier case, in which the court had indicated indirectly that, in a proper case, it might end the requirement of privity of contract.[14] However, the court declined the invitation and held that, even assuming the plaintiff had standing to sue, his claim under an implied warranty was barred because the defect in the machinery was so obvious to the naked eye as to put the plaintiff on notice.[15] Thus the privity rule was bypassed and therefore remains in effect.

V. Defenses

A. Occupied Crossing Doctrine

The past year has seen two exhaustive treatments of the "occupied crossing" doctrine. In both, the court found that while in the ordinary case the railroad has the right to block a crossing with its train without giving any warning to oncoming motorists, the defense was unavailable to the railroad since the crossing in question was of a peculiarly dangerous nature.

Illinois Cent. R.R. Co. v. Williams[16] may be principally remembered as the case where, unfortunately, the railroad company president sent a telegram to the Public Service Commissioners suggesting that the power company owning buildings which formed a background to the crossing be requested to shade its lights to avoid confusing motorists. During the trial, the telegram was allowed in evidence as an admission against interest that a confusing situation did exist. The court upheld a $60,000.00 verdict where the college graduate motorist had a life expectancy of thirty-eight years and was earning $11,000.00 annually. The "unusually dangerous crossing" was unmarked; the tracks were slightly raised and at an angle; approaching cars had to be fairly close by before light beams would strike a box car. There seemed to be

[13]140 So. 2d 558 (Miss. 1962).

[14]E. I. Du Pont De Nemours & Co. v. Ladner, 221 Miss. 378, 73 So. 2d 249 (1954).

[15]For a brief but interesting case on products liability see Campbell Soup Co. v. Duskey, 135 So. 2d 414 (Miss. 1961).

[16]135 So. 2d 831 (Miss 1961).

no doubt that the motorist was driving in excess of the posted speed limits. The chancellor's apportioning under the comparative negligence statute was approved by the court. Admission of evidence of prior accidents at the same crossing was found not to be error. There was non-reversible error in the admission of certain opinion evidence by a policeman and a civil engineer that the crossing was unusually dangerous.

The Supreme Court left no stone unturned in considering the defense in *Green v. Gulf, M. & O. R.R. Co.*,[17] indeed, the case may serve as a primer on the subject of "occupied crossings." It was held here, as in the case above, that the railroad was negligent in not putting a flagman or a warning device in front of the crossing since, under the circumstances, the crossing was particularly dangerous. The elements which the court emphasized were the distinct curve in the road before the crossing, the foggy conditions on the night of the accident, and the fact that the crossing had been blocked for a period exceeding the statutory limit.[18]

B. Sudden Emergency

The sudden emergency doctrine continues as a potent defense. *Majure v. Herrington*[19] gives an interesting instance of its application. It appears that the defendant driver cleared the crest of a hill and was confronted with an automobile bearing down on her in the wrong lane. This unidentified driver was passing a line of cars, so that the defendant's only escape from a head-on collision was to swerve off the highway to the right. In doing this, the defendant lost control of her automobile, swerved back across the road, and hit the lead car in the line. The court held that because of the sudden emergency, the defendant was not held to as high a degree of care as would be required under ordinary circumstances. A judgment entered on a verdict for the defendant was affirmed.

C. Loss of Consciousness

At least one instance during the past year of the failure of liability to attach may be relegated to judicial tolerance for the natural infirmities of the human body. *Dickinson v. Koenig*[20] appears to be the first application in this jurisdiction of the principle that the loss of consciousness on the part of an automobile driver is a complete defense to a charge of negligence or gross negligence, provided that the defendant

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[17]141 So. 2d 216 (Miss. 1962).
[18]Miss. Code Ann. § 7780 (1956).
[19]139 So. 2d 635 (Miss. 1962).
[20]133 So. 2d 721 (Miss. 1961).

could not have anticipated that such unconsciousness was likely to occur. This death case arose when the car in which the plaintiff's decedent was riding left the road and wrecked. The defendant driver had testified that, after attempting to pass the vehicle ahead and being forced to pull back in line, he fainted and remembered nothing further. On the basis of such testimony, a judgment for the defendants was affirmed.

D. Assumption of Risk

The maxim volenti non fit injuria has not lost its vigor as an absolute defense available to the drunken operators of automobiles, as indicated in *Morris v. Lammons*.[21] The plaintiff, owner of the automobile and a passenger therein, sued her sister, the operator, for injuries sustained in a collision. The evidence clearly showed that all the occupants of the car had been drinking. It further showed that the plaintiff knew that the defendant was drunk and driving at an excessive speed, and that the plaintiff made no attempt to take over operation of the vehicle. In affirming a judgment for the defendant, the Supreme Court held that the evidence supported an instruction on assumption of risk given for the defendant. The court also indicated that, even had the evidence been insufficient to allow the jury to consider the defense, the plaintiff could not complain since she was allowed an instruction which mentioned the defense.

May v. Vardaman Mfg. Co.[22] gives a special variant of assumption of risk in those cases of injuries to servants not covered by the workmen's compensation provisions. The plaintiff's husband, a carpenter, was killed when the building on which he was working collapsed. It was held that the employee assumed the risk of engaging in work which, by its nature, was constantly changing its complexion as to the degree of danger. This principle works as an exception to the normal duty of the master to provide his servant with a safe place to work and applies, for example, to the construction, destruction, and repair of buildings.

VI. Evidence

It has been said that the field of contracts is the queen of the law. It might be said with equal justification that evidence is the queen of negligence actions, if not of all trial practice. The following cases represent some recent rulings on evidence, for the most part only briefly noted.

Of personal interest to the writer was *Barham v. Nowell*,[23] which principally concerned the admissibility of motion pictures taken by

[21] 139 So. 2d 867 (Miss. 1962).
[22] 142 So. 2d 18 (Miss. 1962).
[23] 138 So. 2d 493 (Miss. 1962).

detectives showing the plaintiff walking without a limp, running, and engaging in other activities. There was a sharp conflict in the evidence as to whether the plaintiff limped and as to whether he had the permanent injury claimed. The lower court refused to allow the jury to see the pictures because some were not clear enough. The Pendleton detectives were permitted to testify as to what they observed of the plaintiff's activities while the motion pictures were being taken. A proper foundation was laid for the introduction of the film. The essential elements were established, to wit: relevancy of the subject matter to the issues; identity of the subject matter; and proof that the motion pictures represented an accurate and faithful representation of the scenes filmed. On motion of the appellant, the Supreme Court viewed the moving pictures which were sent up with the record. Reversing on the issue of damages only, the court held that the pictures were a vital part of the defense and that the jury should have had the benefit of such evidence. The question of admissibility was a matter addressed to the sound discretion of the trial judge, but the court noted that the judge evidently thought that all the scenes had to be clear enough to identify the plaintiff before any of them would be admissible. The testimony of the detectives would be less convincing than the pictures which were not merely cumulative evidence. This case clears the way for the use of detectives and motion pictures under appropriate circumstances.

Some specific rulings on evidential questions may be of particular help: If a witness sees an automobile speeding about a quarter of a mile away from the accident scene, but does not see it thereafter, the testimony is too remote to be admissible on the issue of proximate cause;[24] a written advertisement concerning the proper operation of a swimming pool chlorinator is rank hearsay and is to be excluded;[25] the defendant can inject the issue of a release and insurance coverage, without fear of mistrial, if the plaintiff demands his $50.00 deductible payment;[26] in a discovery motion, the movant must identify the specific photographs that he wishes to examine and allege what they portray.[27] Further, a policeman may make visual experiments at an intersection and testify about his results even though some of the trees there may have been trimmed subsequent to the accident;[28] a written statement used to impeach a witness does not have to be produced, introduced, or shown to the witness, and the cross-examiner may frame questions directly therefrom;[29] if the plaintiff's orthopedic surgeon is in the courtroom

[24]See, *e.g.*, Denman v. Spain, 135 So. 2d 195 (Miss. 1961).
[25]See, *e.g.*, Pevey v. Alexander Pool Co., 139 So. 2d 847 (Miss. 1962).
[26]See, *e.g.*, Ginn v. Culpepper, 137 So. 2d 179 (Miss. 1962).
[27]See, *e.g.*, Dent v. Luckett, 135 So. 2d 840 (Miss. 1961).
[28]See, *e.g.*, Elliott v. Massey, 134 So. 2d 478 (Miss. 1961).
[29]See, *e.g.*, Anderson v. Sills, 134 So. 2d 482 (Miss. 1961).

ready to testify, and the plaintiff objects to his so doing when called by the opposition, the jury may properly make adverse inferences therefrom.[30] Finally, staged work material photographs are admissible to demonstrate the safe manner of installing church window panes.[31]

VII. Damages

The issue of punitive damages in automobile cases received careful consideration in *Fowler Butane Gas Co. v. Varner*.[32] The defendant driver, after making a delivery for the defendant employer, backed out of a private driveway, and in doing so ran over a small child playing in a sand pile at the edge of the driveway. The driver testified that before backing out he looked down the driveway and believed that the way was clear, but that he was unable to see behind him while operating the truck. He did not know of the minor plaintiff's presence until after he had hit her with the wheels. The suits of the child and the parents were consolidated and resulted in verdicts for both plaintiffs, the child receiving $65,000.00. The Supreme Court required a remittitur of $15,000.00 by the child and $7,500.00 by the parents as an alternative to a new trial. The remittiturs resulted from errors as to punitive damages. The court found that there was ample justification for the belief that the jury's verdict of $65,000.00 contained an award for punitive damages, since the award was large and no instructions on punitive damages were given for the plaintiffs. Moreover, the evidence would not sustain a finding that there was gross negligence on the part of the driver evincing a total disregard for human life. Such finding would assume that the driver did not look where he was going once he started the truck in motion. The court pointed out that the driver had made many such deliveries without incident and that he had looked down the driveway before backing out. As to the claim of the parents, the court reiterated the rule that parents can receive punitive damages for torts committed against a child only in the case of seduction. The refusal of the trial court to grant an instruction for the defendants that punitive damages could not be awarded was found to be reversible error, but the court indicated that the case could be better settled by remittiturs.

Numerous cases might be cited of the reluctant dealings of the Supreme Court with the size of verdicts, but one very instructive decision should suffice. *Rayner v. Lindsey*[33] is especially interesting as a highly

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[30]See, *e.g.*, Pittman v. Mendenhall-Mims Mitchell Funeral Home, Inc., 137 So. 2d 518 (Miss. 1962).

[31]See, *e.g.*, Wright v. Burk Hall-Tayloe Paint & Glass Co., 136 So. 2d 599 (Miss. 1962).

[32]141 So. 2d 226 (Miss. 1962).

[33]138 So. 2d 902 (Miss. 1962).

subjective treatment of the evidence relating to the plaintiff's injuries. After the accident in question, the plaintiff was never unconscious and walked and talked at the scene. He complained that his back was hurting but refused to go to the hospital. Six days later, he went to see Dr. Donald L. Cooper, who was discussed previously in a Louisiana case.[34] Dr. Cooper did not send the plaintiff to the hospital, but advised bed rest at home, claiming that he found much wrong with the plaintiff's back. However, he was not treated according to usual orthopedic methods. The Mississippi court found that the damages were based primarily upon the sympathetic diagnosis of this family doctor who practiced many miles from the metropolitan area where the plaintiff lived. Understandably, the plaintiff had made many long trips to see Dr. Cooper. The trial court's ruling that there would be a new trial unless the plaintiff remitted $15,000.00 of the $60,000.00 was upheld on appeal.

VIII. Insurance

A. Insured Event

The infinite variations of facts out of which personal injury and property damage actions arise have led to close interpretations of insurance policies. In construing these "contracts of adhesion" the court has consistently followed the principle that, while the words of insurance policies should be given their normal and reasonable meaning, ambiguities should be strictly construed against the insurer so as to give the widest coverage possible under the language.[35]

A problem which is likely to be a recurring one is treated in *Wyse v. Dixie Fire & Cas. Co.*[36] The plaintiff was the owner of an automobile which had been entrusted to his son for a pleasure trip. The son had taken along a companion, the latter assuming the operation of the vehicle when the son became sleepy. An accident occurred while the companion was at the wheel. The plaintiff, in an earlier suit, had recovered a judgment against his son's companion. This case arose when the plaintiff attempted to recover under a liability policy covering the father of the negligent driver and the members of his family. The policy specifically excluded coverage of liability for damage to property "in charge of the insured." The court construed the policy in favor of the defendant insurer, holding that the automobile was clearly "in charge of" the driver-guest.

Another instance of defining the insured event appears in *Cox v. Peerless Life Ins. Co.*[37] The plaintiff-insured was an injured bus passenger. While changing busses at a station, she was hit by a passenger

[34]Cooper v. Succession of Cooper, 234 La. 832, 101 So. 2d 686 (1958).

[35]See, *e.g.*, Great Am. Ins. Co. v. Bass, 208 Miss. 436, 44 So. 2d 532 (1950).

[36]136 So. 2d 578 (Miss. 1962).

[37]135 So. 2d 411 (Miss. 1961).

and knocked to the floor of the bus, receiving serious injuries which necessitated hospital treatment. She sued under a family accident and hospital policy which covered injuries caused by a "bus accident." The court held that the term "bus accident" should not be restricted to a casualty to the bus itself. This unusual, undesigned and unexpected occurrence of the fellow passenger's accidentally colliding with her and causing the injury was within the definition. The plaintiff got a new trial.

A more difficult exercise in construction appeared in *Great Am. Ins. Co. v. Tripplett*,[38] which concerned a garage liability policy. There, the injury sustained by the child plaintiff as a result of an explosion of gasoline negligently substituted for kerosene purchased at the service station was held to be due to an "accident" within the meaning of the garage liability policy. The insurer sought to invoke an exclusionary provision which provided that the policy did not apply to any goods or products sold, handled, or distributed. However, the court held that the negligent act of the attendant at the insured station was an operation incident to the business being conducted on the premises by the insured.

Tracing the source of an injury to a proximate cause within the coverage of the policy has been the problem in at least two notable cases. In *State Farm Mut. Auto. Ins. Co. v. Johnson*[39] the decedent, Johnson, while driving across a bridge, found that his right rear wheel had dropped off the edge. Obtaining the assistance of one Odom, they placed a timber under another wheel. Odom then attempted to drive forward while Johnson observed. The wheel spun and threw the plank into Johnson's chest causing his death. His widow sued and the insurer was held liable for the funeral expenses under the provisions of a policy providing coverage for injuries or death caused by an accident "through being struck by the automobile." Admittedly, the automobile threw the plank, and the plank struck Johnson. This indirect chain of circumstances was sufficient for the widow to prevail.

In *Providence Wash. Ins. Co. v. Weaver*[40] a truck owner brought suit on an inland marine policy for the accidental death of live stock while in transit. The plaintiff's trailer had overturned and some of the cattle had escaped. Their tracks led to a nearby river, leading circumstantially to the assumption that they had drowned. The policy in issue covered "direct loss" caused by the overturning of a vehicle. The court held that the jury was justified in finding that the cattle died as a proximate result of the overturning of the vehicle. The assumed drowning was treated as an incidental, rather than a dominant or efficient cause.

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[38] 139 So. 2d 357 (Miss. 1962).
[39] 133 So. 2d 288 (Miss. 1961).
[40] 133 So. 2d 635 (Miss. 1961).

B. Waiver and Estoppel

In view of the now prevalent practice of handling the business of numerous insurers through the office of one agent, the case of *Employers Fire Ins. Co. v. Speed*[41] is of distinct significance. The agent there represented eight insurers and the plaintiff was one of his customers. Determining to make additions to existing buildings, the plaintiff requested the agent to procure insurance on the new facilities which were under construction and the agent orally agreed to do so. Before the agent had done anything by way of acting on his promise, the buildings in question were damaged by wind. The plaintiff brought suit against six of the eight companies represented, basing his claim for recovery on two theories, viz: (1) that the insurers were estopped, through the representations of the agent, from claiming that there was no coverage, and (2) that there was an enforceable oral contract of insurance under which all defendants were liable.

The court rejected both theories. As to the first, the familiar principle that waiver or estoppel cannot be used to extend coverage where there is none by the terms of the policy was applied. As to the second, there was greater difficulty. The court declined to decide whether there could, in fact, be an oral contract of insurance. But assuming that such a contract be possible, it was held that there must be, at the very least, a *designation by the agent of one insurer to bear the risk.* What constitutes "designation" was not decided, but one may presume that a memorandum to a secretary would be sufficient.

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[41] 133 So. 2d 627 (Miss. 1961).

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Student Comments

THAT "SIMPLE AND CLEAR RULE"—THE COMMON LAW RULE AGAINST PERPETUITIES IN MISSISSIPPI

I. Introduction

The scope of this paper is a discussion of the impact of a recent Mississippi case, *Carter v. Berry*,[1] on the law of the transmission of property in this state, particularly with respect to the common law Rule against Perpetuities.

II. The Rule in General

The Rule against Perpetuities is not aimed at restraints on alienation; it is a rule against remoteness.[2] Professor John Chipman Gray's classic statement of the Rule is: "No interest is good unless it must vest, if at all, not later than twenty-one years after some life in being at the creation of the interest."[3] This statement of the Rule is generally accepted by the courts and both *Carter v. Berry* opinions cite Professor Gray's statement.

The Rule is not satisfied by the fact that there are persons in being who can give a complete title to a purchaser.[4] This is obviously true since a too remote interest in a trust is bad, even though the trustee has the power to sell all the property in the trust. The purpose of the Rule is to require that all future interests be finally determined within some period of time and that period of time is the period formulated by the Rule.

> The object of the rule against perpetuities cannot be simply to prevent tying up a particular parcel of land, or other specific thing, as it would seem from the language of many of the books; . . . for it is applied to a legacy of money and also when the trustees . . . have power to change the investment. In such cases, no specific property is rendered inalienable. . . . Even if specific property is not rendered inalienable, the proceeds of the fund can only be applied in one way . . . .[5]

In each case the problem is: What is that period? "It is, too, a

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[1] 136 So. 2d 871, *suggestion of error overruled and modified*, 140 So. 2d 843, *petition for second suggestion of error denied*, 142 So. 2d 13 (Miss. 1962).

[2] Gray, The Rule Against Perpetuities § 2 (4th ed. 1942).

[3] *Id.* § 201. The period of gestation is added, if there is one. See Thelluson v. Woodford, 11 Ves. Jun. 112, 32 Eng. Rep. 1030 (H.L. 1805).

[4] See Carter v. Berry, 140 So. 2d 843, 844 (Miss. 1962); Gray, *op. cit. supra* note 2, at 4. *Contra, In re* Walker's Will, 258 Wis. 65, 45 N.W.2d 94 (1950), since there is no time limit to the vesting of equitable interests in that state if the trustee has a power of sale.

[5] 4 Kent, Commentaries 323 n.1 (14th ed. 1896).

well-established, simple and clear rule," says Professor Gray,[6] but this latest edition of his book takes 833 pages to explain it and there has been enough litigation since 1942 to illustrate that all questions concerning the Rule were not answered therein.

Professor W. Barton Leach's "Perpetuities in a Nutshell"[7] well explains the basic workings of the Rule, but Professor Leach cites Lord Macnaghten as a warning, ". . . it is one thing to put a case like Shelley's in a nutshell and another thing to keep it there."[8] The same warning certainly applies to the Rule against Perpetuities, but it is submitted that Professor Leach's attempt to summarize the workings of the Rule comes closer to that purpose than any other like treatise and is probably the ideal starting point for one analyzing a perpetuities problem.

III. Carter v. Berry

Russel B. Johnston of Lowndes County, Mississippi, died testate possessed of large holdings of real estate, dominant holdings in several corporations, other stocks, cash and other personalty. He was survived by an estranged wife, two married daughters and three grandchildren. Insofar as is applicable to this discussion of the Rule, Johnston left 80 percent of his estate to trustees, to continue and accumulate as an active trust and to terminate "when my youngest grandchild (whether now or hereafter born) shall become 25 years of age; provided that in no event shall said trust continue for a longer period than 35 years from the date of this" will, which was 1955. Johnston died in 1958. Upon termination of the trust, the assets were to be "transferred, delivered over, divided and distributed by my trustees to my said grandchildren per capita." The will gave trustees discretionary powers to expend income and corpus for the support, maintenance and education of the grandchildren and such expenditures were to be charged against each grandchild's final share. A spendthrift provision sheltered the trust from creditors of the beneficiaries and the right of the beneficiaries to alienate their interests was suspended until final distribution. The will stated that no provision was made for the testator's two daughters "for the reason that I have heretofore made . . . adequate provisions for them with TRUST AGREEMENTS. . . ." The trusts previously settled consisted of a substantial portion of testator's worth.

In the first opinion by Justice Lee the court held that the interests given to the living grandchildren were vested as of testator's death, but gave no opinion as to participation by any grandchildren born after testator's death. Of course when an interest "vests" or "will vest" is a question of interpretation of the instrument, but "[i]f reasonably pos-

[6]Gray, *op. cit. supra* note 2, § 870.

[7]51 Harv. L. Rev. 638 (1938).

[8]Van Grutten v. Foxwell, [1897] A.C. 658, 671.

sible, the Court will so construe an ambiguous instrument as to render it not invalid under the Rule against Perpetuities. . . ."[9] Once it is decided that the living grandchildren took a vested interest at testator's death, any interest to future grandchildren would necessarily vest upon their birth and within the Rule's requirements, since it is clear that the daughters, at least, are "lives in being,"[10] and "no future grandchild could be born to testator later than the time when the survivor of his two daughters died (with the possible addition of a nine months gestation period). . . ."[11]

But a reading of the first opinion gives one the impression that the court considered that the period within which all interests must vest is a period in gross of 21 years from testator's death, as was the holding of the lower court.[12] If this were the case, the interests to unborn grandchildren could vest more than 21 years after testator's death and would be too remote. In holding the gift valid (but not recognizing the daughters as lives in being) the first decision ignored the doctrine expressed in *Leake v. Robinson*,[13] discussed later in this paper.

However, if the interests vested *in interest* in the living grandchildren the *time of distribution* is immaterial and no class gift problems need be considered since any future interest to unborn grandchildren would necessarily vest during their mothers' lives. If the interests are vested in living grandchildren, even orthodox Rule against Perpetuities doctrines would hold the whole gift valid, since any interest later to vest in other grandchildren (which would partially divest the already vested interests of born grandchildren) would vest within the Rule, i.e., within lives in being. The 21 years is not needed.

In other words, the first opinion is correct, but probably for the wrong reasons. If the interests to born grandchildren are vested (which is not answered in the second opinion), then *all* interests will vest, if at all, during the daughters' lives, since all children are born within their mothers' lives. If the interest vests *in interest* on birth, distribution could be put off indefinitely, as far as the Rule is concerned, so the 25 year old requirement is immaterial.

The second opinion[14] is the difficult one. This opinion, by Justice Ethridge, is in the alternative. "On both foundations [vested or contin-

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[9]136 So. 2d at 874. *Contra, e.g.*, Carter v. Sunray Midcontinent Oil Co., 231 Miss. 8, 94 So. 2d 624, 638 (1957), where the court uoted GRAY, *op. cit. supra* note 2, § 629: "Therefore every provision in a will or settlement is to be construed as if the Rule did not exist, and then to the provision so construed the Rule is to be remorselessly applied." See also Lazard v. Hiller, 145 Miss. 449, 110 So. 855 (1927); Scott v. Turner, 137 Miss. 636, 102 So. 467 (1925).

[10]140 So. 2d at 848.

[11]*Id.* at 849 (The Case of the Prolific Female Decedent?).

[12]*Id.* at 848.

[13]2 Mer. 363, 35 Eng. Rep. 979 (Rolls. 1817).

[14]Carter v. Berry, 140 So. 2d 843 (Miss. 1962).

gent], we hold that the gift to the grandchildren is valid."[15] It holds (1) the interest in each grandchild vested in each existing grandchild at the testator's death and will vest in unborn grandchildren upon their birth, thus no interest will be too remote, but (2) if the interests are not vested but contingent on the grandchild's surviving until the youngest reaches 25, the will is modified by "equitable approximation" so that the trust will terminate when the youngest grandchild (living or hereafter born) reaches 21, but in no event longer than 35 years from the date of the will.[16] Thus, all interests will vest, if at all, within 21 years after the death of the survivor of two daughters.

In support of the second conclusion, the court relied on a New Hampshire case decided in 1891.[17] In that case there was a gift to grandchildren who should be living when the youngest should reach the age of 40. Chief Justice Doe conceded (as did Justice Ethridge here) that the contingency was too remote, conceded that the direction to postpone vesting until the youngest reached 40 was "illegal" by 19 years, but said that postponement of vesting until the youngest reached 21 years of age would not be "illegal." So, by the doctrine of *cy pres,* the 40 year contingency was reduced to 21. Justice Doe said that the express declaration in the will, "if my intention, herein written, cannot operate to its full extent, it shall take effect as far as possible," was superfluous, as the law renders the gift valid *cy pres.* No such express declaration is included in Johnston's will, but the court evidently agreed that it is included as a matter of law.

IV. "Rejection" of Leake v. Robinson

The "all or nothing" rule of *Leake v. Robinson* is: If a contingent interest of any member of the class to whom the gift is made may vest too remotely, the whole gift is bad (even though some interests would otherwise vest, if at all, not too remotely). The idea is that no interest can "vest" (as the term vest is used in perpetuities cases) until all interests in the class gift vest. A gift to a class is one gift, and, for purposes of the Rule, the gift does not "vest" until all participants are determined. If one member of the class meets the contingency within the period, his interest is not finally "vested" until it is determined that such share (fractional share of the gift) will not be diminished by an additional member's meeting the contingency. If it is possible that such other interest will vest too remotely, the whole gift falls.

In applying this rule a court first determines, by construing the instrument, who make up the class. (In *Carter v. Berry,* this problem is foreclosed—the testator expressly included all his grandchildren, born

[15] *Id.* at 850.

[16] *Id.* at 856.

[17] Edgerly v. Barker, 66 N.H. 434, 31 Atl. 900 (1891), 28 L.R.A. 328 (1895).

or unborn.) Then the court must decide on what contingency each interest would meet the condition. (Here, in the second phase of the alternate holding, the court implied that the condition was survival until the youngest reached the age of 25.) Then, if the condition as to any member may be fulfilled too remotely, the gift fails.

In *Carter v. Berry* it is possible that an unborn grandchild might not reach 25 until 21 years after the death of *anyone* in being at testator's death. It is possible that only unborn grandchildren will ever reach 25. Thus, it is possible that the only grandchildren who meet the condition are those who will meet it at a time too remote and, regardless of *Leake v. Robinson* the whole gift would fall. *Leake v. Robinson* was a case where the gift was to Robinson's children who should reach 25, not to his children in being when the youngest reached 25. However, the philosophy is treated as the same. It is possible that the unborn grandchildren might reach 25 more than 21 years after all lives in being. But the trouble is, if the gift were struck down the testator's two daughters (the wife's claim had been settled) would take, *and this was expressly against his wishes.*

As set out above, the *Carter* case is different from *Leake,* because in the former the interests were to vest all at once in those grandchildren alive when the youngest reached 25. In the latter, the interest was to vest in each beneficiary when he reached 25. The distinction is this: In *Leake,* possibly some would meet the condition not too remotely, then others too remotely; in *Carter* since all beneficiaries will meet the condition at one time, all interests will vest either within the period or all too remotely. This writer submits that *Carter* is not "a situation in which there is a valid vested interest subject to partial divestment by an invalid gift"[18] since no vested interest will be partially divested by the too remote vesting of another interest. No one meets the condition until all meet the condition.

In short, *Leake* holds: no interest vests until all vest. But the will in *Carter,* as interpreted, said that by its own terms. One need not apply the *Leake* doctrine to reach that result. So, why worry about *Leake*?

Admittedly, it is a situation where some of the grandchildren (those living at testator's death) will meet the condition, if at all, within the period but their contingent interests are defeated by the possibility that none will meet the condition within the period. In principle, the policy toward "curing" the gift may be the same, but this situation does not have the surface appeal of one in which a beneficiary loses an otherwise vested interest because another's might vest too remotely.

One must assume that the express statement in the opinion that "the

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[18]140 So. 2d at 851.

lives in being in the will are those of Johnston's two daughters"[19] should be modified by the phrase "at least." This conclusion is drawn since the court elsewhere in the opinion states, ". . . the court could find that the gift was valid as to the donees living at the time of creation of the interest, here the three then-living grandchildren, and could eliminate unborn children [grandchildren?]."[20] Unless the three grandchildren are their own "lives in being," the gift would be invalid even as to those then living if the contingency were that they be living when the youngest reaches 25, since one of the grandchildren was less than 4 years old at testator's death. But surely, beneficiaries born at the time the interest is created are their own "lives in being."

The court does not reject *Leake v. Robinson,* but changes the gift so that it cannot violate the Rule, thus avoiding rather than rejecting the *Leake* doctrine of "infectious invalidity."[21] "Rejection" of *Leake* would require the elimination of those beneficiaries to whom the contingency was too remote. This was not done. Even those who may never meet Mr. Johnston's contingency validly are included. Unborn grandchildren are included and the gift to them is made valid by the doctrine of "equitable approximation."

V. Equitable Approximation

Rather than eliminate those of the class whose interest might vest too remotely, the court changed the contingency upon which the beneficiaries could take, by the use of the doctrine of "equitable approximation." Equitable approximation has been distinguished from *cy pres* by the Mississippi court:

> At this point it should be observed that the cy pres practice is not to be confused with the doctrine of equitable approximation which has grown up in the judicial administration (as distinguished from judicial creation) of charitable trusts. . . . Their purpose and their application are entirely different. As said by the Alabama court (Lovelace v. Marion Institute, et al., 215 Ala. 271, 110 So. 381), "The appeal in this case is not to any cy pres power of the court but to the equitable doctrine of approximation, in virtue of which the court of chancery exercises jurisdiction merely to *vary the details of administration,* in order to preserve the trust, and carry out the general purpose of the donor."
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> But the jurisdiction of courts of equity to supervise the execution of trusts *does not include the power to alter the*

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[19] *Id.* at 848.
[20] *Id.* at 851.
[21] *Id.* at 850.

> *terms of the trust.* Morris v. Boyd, 110 Ark. 468, 162 S. W. 69, Ann. Cas. 1916A, 1004. (Emphasis added.) [22]

And later, per Justice Ethridge:

> A trustee may be permitted by the Chancery Court to deviate from a term of the trust if owing to circumstances not known to the settlor and not anticipated by him, compliance would defeat or substantially impair accomplishment of the purposes of the trust. . . . This rule permitting *deviations* from the settlor's directions *as to mere methods of administration* where the charitable objective is not changed but rather the means and methods of it are varied, sometimes called the equitable doctrine of approximation, must be distinguished from the cy pres power. That is the principle that equity will, when a charity is illegal or later becomes impossible or impractical of fulfillment, substitute another charitable object which is believed to approach the original purpose as closely as possible. This latter theory that equity has the power to mould the charitable trust to meet emergencies was rejected and held to be not applicable to the facts in National Bank of Greece v. Savarika, 167 Miss. 571, 148 So. 649 (1933). (Emphasis added.) [23]

So, in the *Carter* case the court relied on the doctrine of "equitable approximation," rather than prerogative *cy pres*.[24] "The dominant idea of the entire will [was] that testator's grandchildren should have the bulk of his estate. . . . The *time* when the grandchildren should have the estate was secondary and subordinate to the intent that they should have it. . . . The *time* is changed. . . .The twenty-five years are reduced to twenty-one by testator's general approximating purpose and dominant interest. (Emphasis added.) [25]

The inference is that, since only the time of taking is changed, only the method of administration of the trust is changed. *But are not the beneficiaries changed and void interests given to other beneficiaries who could otherwise validly take—and on a different contingency, at that*? No better analysis of this problem can be made than that by Professor Gray in his criticism of the decision in *Edgerly v. Barker*:

> The doctrine of the New Hampshire court in this case involves a fallacy. It speaks of a primary intent to give to persons and a secondary intent to give to them at a particular time, and it purports to preserve the primary intent while discarding the secondary intent by substituting another time. This assumes that the persons remain the same, and only the time

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[22]National Bank of Greece v. Savarika, 167 Miss. 571, 593, 148 So. 649, 654 (1933).

[23]Mississippi Children's Home Soc'y v. City of Jackson, 230 Miss. 546, 554, 93 So. 2d 483, 486 (1957).

[24]In the United States *cy pres*, or approximation, is applicable not only to charities but also to all devises and contracts wherein the future is provided for. It is an essential element of equity jurisdiction. 10 AM. JUR. *Charities* §§ 123-24 (1957).

[25]140 So. 2d at 855.

> changes. But that is precisely what does not occur; with the time, the persons are changed. Take the present case. The testator meant to give to those of his grandchildren who reached forty; the court gives the property to those who reach twenty-one. There may be six grandchildren who reach twenty-one, and only one who reaches forty. In such case shares would be given to five persons whom the testator never meant to have it. There may be some answer to this, but it is a real and very serious objection, and deserves an answer, and it gets none from the New Hampshire Court. The case is dealt with throughout as if the only question were whether the same persons should get the property at forty or at twenty-one.[26]

One will observe that if only the time changes, the interests necessarily are vested (or would vest on birth) and the Rule is not violated by *payment* when the youngest attains 25. If such is the case, the will need not be rewritten to give validity to the gift; it is valid as it stands. The effect of vesting in this case is that if the beneficiary dies after the interest vests, but before it is distributed, the interest is not lost. His heirs or beneficiaries under his will take the share rather than the rest of the class. To hold the interests contingent but change the time of vesting is something more than "deviations . . . as to mere methods of administration."[27] It may change the beneficiaries. It is submitted that the court has deviated from its own definition of "equitable approximation" and has applied what it formerly called "prerogative *cy pres*."

VI. Impact of the Case on Mississippi Law

A. Our "Donee Statute"

Why is our "Donee Statute"[28] not discussed? The trust contained a large amount of Mississippi realty. The only mention of this problem is the statement, "We are not concerned here with the 'succession of donees' statute. Miss. Code 1942, Rec., Sec. 838; see Custy and Brand Future Interests—The Mississippi Two Donee Statute and The Common Law Rule Against Perpetuities, 30 Miss. L. J. 221 (1959)."[29] Be that as it may, it is again clearly indicated that the common law Rule

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[26]Gray, *op. cit. supra* note 2, § 872.

[27]Mississippi Children's Home Soc'y v. City of Jackson, 230 Miss. 546, 555, 93 So. 2d 483, 486 (1957).

[28]Miss. Code Ann. § 838 (1956).

[29]For discussions illustrating the divergent views as to this statute, both the old "Two Donee" and present "Succession of Donees" versions, see Gray, *op. cit. supra* note 2, § 746 n.1; 2 Simes & Smith, The Law of Future Interests § 1437 (2d ed. 1956); Custy & Brand, *Future Interests—The Mississippi Two Donee Statute and the Common Law Rule Against Perpetuities*, 30 Miss. L.J. 221 (1959); Dulaney, *The Two Donee Statute*, 1 Miss. L.J. 398 (1928); Holmes, *Some Observations on Statutory Rule Against Perpetuities*, 4 Miss. L.J. 122 (1931); Smith, *Mississippi's "Odd and Confused Statute,"* 2 Miss. L.J. 228 (1929).

against Perpetuities also applies to land as well as personalty in Mississippi;[30] and since the final gift would be a legal interest rather than an equitable one it would seem immaterial that this case involved a trust. The question as to whether the "Donee Statute" is inapplicable or whether it merely is not violated is not anywhere answered in the decision and that question is beyond the scope of this paper.

B. What Does the Case Hold?

Since the case holds the gift valid, one cannot say that it expressly holds that the Rule is in effect in Mississippi as to realty. Also, since the holding is in the alternative, what is the "law of the case"?[31] The gift was held valid whether vested or contingent, so one cannot say that the case holds either.

"The twenty-five years refers to the time of distribution not to vesting. . . . If a grandchild dies before the time of distribution his heirs inherit his share. . . . He [testator] did not say that the grandchildren should receive a share when and if they lived until the youngest . . . attained twenty-five."[32] Under this alternative the shares vest upon birth (or are vested on testator's death as to grandchildren then born) and the daughters may yet receive a share if one of the grandchildren dies (or one is born and then dies) prior to distribution.

On the other hand, the decree was modified to read "except by equitable approximation the trust shall continue and terminate when the youngest grandchild . . . shall become twenty-one. . . ."[33] which was unnecessary to save the gift if the interests are not contingent upon survival to the time of distribution. If the interests are contingent upon survival, the death of any grandchild terminates his interest and his heirs receive nothing.

On another trial (in case a grandchild dies before distribution) the court could decide any one of the following: (1) the interest "vested" upon the grandchild's birth (or date of testator's death as to then living grandchildren) and his heirs take his share (alternative I); or (2) the interest would vest when he reached 21 and was to be distributed when the youngest reached 21, so any grandchild dying under 21 has no "vested" interest, but if he had reached 21 he does, and inheritability depends upon the grandchild's age at death. (This possible construction was not discussed in either decision); or (3) no interests vest until all

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[30]See McCormack v. Blanks, 226 Miss. 767, 85 So. 2d 204 (1956) (dictum), 28 Miss. L.J. 88.

[31]For a discussion of this term see Continental Turpentine & Rosin Co. v. Gulf Naval Stores Co., 142 So. 2d 200 (Miss. 1962). "It relates entirely to questions of law. . . ." *Id.* at 207.

[32]140 So. 2d at 849.

[33]*Id.* at 856.

vest (when the youngest reaches 21), so no grandchild has an inheritable interest until he receives it (alternative II); without deviating from the "law of the case" doctrine. One could say that the whole decision is dictum, except insofar as it holds the gift valid and that the daughters receive nothing. The question of inheritability (vested *vel non*) of the shares is not foreclosed by this decision.

C. Different Case: Age Not the Too Remote Contingency?

Take this case: To all of A's grandchildren (now or hereafter born of parents now or hereafter born). Suppose A is living at the creation of the interest. The interest to any of A's grandchildren (now or hereafter born) by A's children in being at the creation of the interest would not be too remote, since such grandchildren would be born within lives in being (their parents). But the interests to A's grandchildren born of A's children not in being at the creation of the instrument would be bad. Would the court (by "equitable approximation") limit the class to grandchildren of A born of parents in being at the creation of the interest, a clear rejection of *Leake v. Robinson*? This would leave out grandchildren by A's later born children, and the donor specifically said *all* grandchildren. It is more apparent in such a case that the class is changed, not just the time of taking. How would the court dispose of the "bad" interests? How could it tell (until possibly well after the time formulated by the Rule) how many "bad" shares there would be? All it could do would be to limit the class to those who could validly take otherwise.

Such a case is no different, in principle, from *Carter v. Berry*, but the changing of beneficiaries is more apparent. However, the court indicates that it would do just that.[34] It insists that the question is one of separability, not of application as a rule of law, as Professor Leach insists,[35] rejecting the orthodox notion that the purpose of the Rule against Perpetuities is to defeat intention, not assist it, if the intention is to create an invalid perpetuity. Of course, in defense of the savings rule, Mr. Johnston intended to create no such thing. If he had known his gift was invalid as made, he would not have made it that way. It is submitted that *no one* can be presumed to know perpetuities law.[36]

D. In General

At least the case *indicates* that (1) the common law Rule against Perpetuities applies to Mississippi realty and (2) the court will not be

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[34]"If this [cutting out unborn grandchildren] were the only choice, we would not hesitate to take it." 140 So. 2d at 852.

[35]Leach, *The Rule Against Perpetuities and Gifts to Classes*, 51 HARV. L. REV. 1329 (1938).

[36]See Lucas v. Hamm, 56 Cal. 2d 583, 364 P.2d 685 (1961).

reluctant to abandon the historical concepts of application of the Rule if the court thinks the testator would have preferred an "approximation" of his intentions rather than intestacy. "Certainly the problem is one of separability, not of application of a rule of law. It is a question of construction, not of application of a rule of law."[37] So the court anticipates that in any case in which a gift is invalid under the Rule it will cut it down to size so that it does not violate the Rule, if the general intent of the testator as expressed in the will indicates that he would prefer that result to invalidity of the gift. Whether this policy is advisable or not is discussed in Section VII of this paper.

VII. The Rule As Policy

Page after page has been written on the question of why a rule such as the Rule against Perpetuities should or should not strike down the otherwise valid gifts of testators or settlors. On the one hand (strike them down!) are the common law cases since the late seventeenth century.[38] On the other hand (save them!), is, in the main today, W. Barton Leach, Story Professor of Law, Harvard Law School, who has waged an unrelenting campaign to "stay the slaughter of the innocents."[39] And he has been notably successful in his efforts. He is convincing, sincere in his purpose, very skilled in the use of words and especially good at getting at the root of the problem:

> The difficulty with any mathematical rule is that it tries to state substance in terms of form. Two consequences inevitably follow. In the first place, the skillful will be enabled to commit sins of substance while bringing themselves within the mathematical requirements—and few will deny this is a fair description of a gift "to all my descendants as shall be living 21 years after the death of all the descendants of Queen Victoria living at my death." In the second place, the inept will frame dispositions, not inherently unreasonable in such a fashion that the mathematical rule is transgressed—and I submit that this is a fair description of a gift "to A for life, remainder to such of his children as reach 25." The frequency of such gifts is evi-

[37]Carter v. Berry, 140 So. 2d 843, 852 (Miss. 1962).

[38]The Duke of Norfolk's Case, 3 Ch. Cas. 1, 31, 22 Eng. Rep. 931, 949 (1682) is generally recognized as the beginning.

[39]From his own list in Leach & Logan, Future Interests and Estate Planning (1961); 6 American Law of Property § 24.11 (Casner ed. 1952); Leach & Tudor, The Rule Against Perpetuities (1956); American Bar Ass'n, Legislators' Handbook on Perpetuities 24 (1958); Leach, *Staying the Slaughter of the Innocents*, 68 L.Q. Rev. 35 (1952); Leach, *Perpetuities in Perspective; Ending the Rule's Reign of Terror*, 65 Harv. L. Rev. 721 (1952); Leach, *Perpetuities Legislation, Massachusetts Style*, 67 Harv. L. Rev. 1349 (1954); Leach, *Perpetuities Reform by Legislation: England*, 70 Harv. L. Rev. 1411 (1957); Leach, *Perpetuities: New Absurdity, Judicial and Statutory Correctives*, 73 Harv. L. Rev. 1318 (1960); Leach, *Perpetuities Legislation: Hail, Pennsylvania!*, 108 U. Pa. L. Rev. 1124 (1960).

> dence of their naturalness and reasonableness. It is all very well to consider that manhood had been attained by a tough-fibred youth of twenty-one when the chief duties of a man were to wield a sword, wear a tin suit, collect feudal dues from the tenantry and torture gold out of the usurers, but it hardly follows that a Junior in college is competent to handle investments in a world of Coolidge booms, Hoover depressions, Roosevelt recessions and planned economy [and the New Frontier?].[40]

This is the heart of the problem: The Rule is mathematical and unbending; people, their thoughts, wishes and desires are not. Take *Carter v. Berry*. With a little effort, the trust could have been held open for probably 100 years. But Johnston wanted the trust held open for only 32 years. He could not do this, *as the will was worded,* because it is mathematically possible that no "lives in being" would live another 11 (32 minus 21) years. Certainly it is not probable, but not at all certain. And the Rule requires certainty.

But the answer to this seemingly ridiculous situation is: If one wants to leave his property to those whom he chooses, he must do so within the law. Law is not perfect; it can't be. It is necessarily objective, not subjective. The conflict of policy here is the age-old conflict between justice and certainty.

Most everyone (including Professor Leach) feels that there must be some limit on the time within which future interests can be finally ascertained. This is the policy, on the one hand. On the other, most everyone feels that the intention and wishes of a testator should be respected, if they are within the law, and some feel that in certain cases a *technical* rule should not defeat his interests, if there is no real reason to do so. But how can we decide which policy is overriding?

As analyzed by Professor Gray in the preface to the first edition of his book, the policy of certainty is not doubted:

> In many legal discussions there is, in the last resort, nothing to say except to say that one judge or writer thinks one way, and another judge or writer thinks another way. There is no exact standard to which an appeal can be made. In questions of remoteness this is not so; there is for them a definite, recognized rule: if a decision agrees with it, it is right; if it does not agree with it, it is wrong. In no part of the law is the reasoning so mathematical in its character; none has so small a human element.[41]

If we assume that there must be *some* limitation (as most everyone does) on the creation of future interests, we have the next question. Should the restriction be a rigid rule, such as "lives in being plus 21

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[40]Leach, *The Rule Against Perpetuities and Gifts to Classes*, 51 HARV. L. REV. 1329, 1332 (1938).

[41]GRAY, *op. cit. supra* note 2, at xi.

years" or should it be something like "a reasonable time"? Of course, the latter rule might create chaos in the law of property. But, assuming either, on to the real question: What happens if the Rule is violated? There are two general choices: (1) strike the gift down, or (2) cut it down to size. Herein lies the argument.

First, one must consider the reasons for the Rule in today's society. The Restatement of Property gives the following: (1) The Rule provides an adjustment between the desire of the current owner of property to prolong indefinitely into the future his control over it and the desire of the future owners to be free of the dead hand. (2) It contributes to the probable utilization of the wealth of society. (3) It aids in the keeping of property responsive to the needs of its current owners.[42] Property which is "tied up" cannot be used in the tradition recognized by the Anglo-Saxon world—a tradition which stresses individualism and competition.[43]

A further reason for a limitation on the time in which the ownership of equitable future interests must be determined (even though trustees have a power of sale) is that property or assets held in trust may not be so freely used as property owned outright. Our Anglo-Saxon traditions have stressed individualism, self-reliance and freedom and are founded on the basis that every man is his own best judge of what to do with that which he owns. Holding property in trust for some purposes is undeniably desirable, but what earthly reason is there for tying up property longer than 21 years after the death of all those living? How can one know that some unborn person will need protection from his own weaknesses, as one might well know about a naive wife or a ne'er-do-well child? It is just not necessary. Spendthrift and indestructible trusts are bad enough.

The policy is not just to limit restrictions on alienation. It also seeks to limit restrictions on the enjoyment of property. Most testators or settlors don't want to break the Rule. They just don't mean to—they make a mistake. Perhaps a few wish to create a memorial to themselves, or to create the possibility that remote descendants or beneficiaries can live a life of no responsibility, but few people purposefully attempt this. So, criticism of the Rule is not really leveled at its purpose, but at its sometimes unreasonable results[44]—as a strict application

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[42] RESTATEMENT (FOURTH), PROPERTY 2129-33 (1944).

[43] *Cf.* SIMES, PUBLIC POLICY AND THE DEAD HAND at 58 (1955); "[The Welfare State] is not organized on a theory of survival of the fittest, but of survival of the weak."

[44] See, *e.g.*, Loring v. Blake, 98 Mass. 253 (1867) (The Case of the Unborn Widow); *In re* Wood, [1897] 3 Ch. 381 (The Case of the Magic Gravel Pit); Jee v. Audley, 1 Cox 324, 29 Eng. Rep. 1186 (1787) (The Case of the Fertile Octogenarian); *Re* Gaite's Will Trusts, [1949] 1 All E.R. 459 (Ch.) (The Case of the Precocious Toddler).

of the Rule may have caused in *Carter v. Berry*. This is the main argument of the cut-it-down-to-size group. But, if this is to be done, *who will ever raise the question*? The only way the policy behind the Rule can be implemented is by somehow enforcing the Rule. If it is not enforced, who will pay any attention to it?

Suppose a gift which violates the Rule gives the property to ones other than those who would take by intestacy? Will the testator's heirs waste their time and money in bringing suit *so as to cure the gift for their opponents*? Will those who take invalidly raise the question? If they do, they may lose their interests if "equitable approximation" is deemed not applicable. Whether to sue or not will depend on how badly the rule is broken, not whether it is broken.

It is submitted that such a never-never land between good and bad (or rather, cut-it-down-to-size and strike-it-down) is a further complication of an already very complex problem. If the Rule is not deemed desirable, why not do away with it—or change it? It is not a trite statement that "[T]he Rule . . . is a positive rule to defeat intention."[45] Nor is it vindictive. If testator's intentions are contrary to a rule of public policy, then the policy of giving effect to testator's intentions is overridden. Certainly, the Rule is designed to defeat intention and are not all rules of law which make gifts void? If the policy behind the Rule is outdated or if the Rule is too strict, the difficulty is with the Rule itself, not with its enforcement. But one writer suggests[46] that in the United States not more than three or four testators or settlers a year are "frustrated" by their gifts' being invalidated by the Rule. Is this too high a price to be paid for enforcement of the Rule? Usually, it is a bad will that frustrates the testator, not the "bad" Rule. It is submitted that the policies behind the Rule are not outdated and that there must be a penalty for its violation.

It is suggested by some that the penalty should not fall on "innocent" intended beneficiaries. But do they really suffer a penalty? How can one say, if a gift be declared invalid, that refusing to give effect to a void gift is a penalty on the intended beneficiaries? They have lost nothing, except something they never had to start with. Of course, someone other than those testator had intended get the property. But, as said before, not very often. And the recipients are usually the heirs-at-law (so maybe the same intended beneficiaries take, but on valid terms). Whoever suffers the penalty is certainly frustrated, whether one says the testator or intended beneficiaries are the ones who suffer. But in any lawsuit, one side wins and the other loses. Are the losers "penal-

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[45]GRAY, *op. cit. supra* note 2, § 883.

[46]Waterbury, *Some Further Thoughts on Perpetuities Reform*, 42 MINN. L. REV. 41 (1957).

ized"? Not if the decision is socially "correct"—they just pay (or don't receive) as society dictates.

A few states have attempted to solve the problem by legislation[47] varyingly using wait-and-see, second look and *cy pres* methods. The purpose of all this legislation is to prevent the "penalizing" of intended beneficiaries. Rather than commenting on the Pennsylvania or Massachusetts "reforms" it would seem that one should quote a Yankee law professor:

> To return to the Massachusetts Act, it would seem as local as that of Pennsylvania. One who has sojourned in metropolitan Boston for a time is struck with the atmosphere of settled wealth. The adventurous spirit that once marked the Salem clippers seems nothing but a nostalgic memory. Trusts, and these are likely to be spendthrift trusts, are the order of the day. The estate planner is king. But this is not the atmosphere of most of the rest of the United States. Adventure still lurks. The intention of the settlor is not a jealous god to be obeyed at all hazards. The estate planner is not king. Massachusetts and Pennsylvania may well be a law unto themselves. Their perpetuity acts, it is believed, are not for import.[48]

Is this not a fair statement of the problem in Mississippi? Perhaps Mississippi's change in attitude[49]—as may be true elsewhere—is based on a recognition of the fact that often today the reason for setting up future interests is to avoid estate taxes rather than to "tie up" property.

Since as a matter of policy the court decided the gift should be upheld there are alternate methods which could have been used to hold it valid. Some of them are discussed below.

VIII. Other Methods of Upholding the Will

A. Wait and See

This doctrine has been adopted by statute in some states.[50] Rather than decide the validity of the gift on the basis of all possible future events, the court will "wait" and decide the validity on the basis of actual events. In *Carter v. Berry*, for example, if as a matter of fact the youngest grandchild reaches 25 within 21 years after the death of all

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[47]*E.g.*, Conn. Gen. Stat. Ann. §§ 45-95, 96 (1960); Idaho Code Ann. § 55-111 (1947); Mass. Gen. Laws Ann. ch. 184A, §§ 1-2 (1955); Me. Rev. Stat. Ann. ch. 160, §§ 27-28 (Supp. 1959); Pa. Stat. Ann. tit. 20, §§ 301.4-1.5 (1950); Vt. Stat. Ann. tit. 27 § 501 (1959); Ky. Acts 1960, ch. 167.

[48]Bordwell, *Perpetuities from the Point of View of the Draughtsman.* 11 Rutgers L. Rev. 429 (1957).

[49]See Custy & Brand, *supra* note 32, where the collected cases indicate that Mississippi courts previously showed little reluctance in striking down invalid interests.

[50]*E.g.*, Pa. Stat. Ann. tit. 20, § 301.4 (1950).

"lives in being" the gift would be valid under such a rule; if not, it falls. The chances are overwhelming that such would be the case. The only situation in which the gift would turn out to be not valid under such a rule would be if all lives in being die before the youngest afterborn grandchild reaches 4 years old. There is no real objection, in the opinion of this writer, to such a method. After all, the drafter of the will could have inserted a built in "wait and see" clause. See IX. a. of this paper.

B. Variation of the "Equitable Approximation" or *Cy Pres* Method

Since the purpose of "equitable approximation" is to give as much force to testator's intent as is legally possible, this intent could have been approximated a little closer. The decree could have been modified to read "except by equitable approximation the trust shall continue and terminate 21 years after the death of the survivor of testator's two daughters and his grandchildren living at his death (who this writer submits are 'lives in being'), if said trust is not terminated before that time by its own terms." The difference in this and "when the youngest grandchild (whether now or hereafter born) shall become twenty-one" is that in the former the trust will not terminate until the youngest reaches 25 (testator's intention) unless that time turns out to be too remote (or unless 35 years from the date of the will occurs prior to that time). The testator's intent is more closely approximated.[51]

C. Lives in Being Plus 25 Years

If the period of the Rule is not appropriate in modern society, the court could modify it so that it would be appropriate. The books are full of cases in which the Rule is violated because the testator or settlor did not want beneficiaries to take unless they reached 25, which was 4 years too much. If the general consensus is that financial maturity is now reached at 25 rather than 21, then the law could well recognize this feeling. At least one state has done so by statute[52] and another allows "lives plus 30 years."[53] Such a modification would probably save many gifts but still give effect to testators' desires. Certainly four more years would not do much harm, especially since the skilled draftsman can word the condition so as to allow valid vesting up to a century or more with "lives plus 21."[54]

But suppose then the testator specifies "when the youngest of my

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[51]This method has been adopted by statute in some states, *e.g.*, VT. STAT. ANN. tit. 27, § 501 (1959).

[52]IDAHO CODE ANN. § 55-111 (1947).

[53]WIS. STAT. § 230.15 (1959).

[54]See *In re* Villar [1928], 1 Ch. 471, where the testator died in April, 1818, and the estate was finally closed in May, 1918.

grandchildren (whether now or hereafter born) reaches 26 years of age; then we are right back where we started.

D. Reduction of Contingency

Reduce the contingency to 21 without determining whether testator would have so desired or not in any case where the gift otherwise would be void for remoteness because such interest is contingent upon any person's attaining or failing to attain an age in excess of 21.[55]

IX. Conclusion

The law of perpetuities is no more clear in Mississippi today than before *Carter v. Berry*; if anything it is more complex. Not only do we have the question: Is the gift valid? but also: If not, then what? Lawyers drawing wills and trusts can be certain of one thing only: the Rule can jump out of the darkest corners and, at least, cause much unnecessary litigation, expense, heartbreak and ill feelings. It also may cause the draftsman personal expense.[56]

Even if the Rule is applicable to Mississippi realty, even if the courts will continue to use liberal "equitable approximation" techniques, even if the gift is finally sustained, the result will always depend on the court's ideas of what the deceased would have done if he had known the law. Moreover, most other state laws are not so sympathetic to invalid gifts.

Several suggestions may be made as to a common-sense approach to foreclosing the problem before it appears. One can always "rig" the instrument so that, by the terms of the instrument, the Rule cannot be violated. Or one can expressly give directions as to what is to be done with gifts which do violate the Rule. The former suggestion is probably more fool-proof, but the latter may allow the testator or settlor more freedom in distributing the property, so long as the alternate gift does not violate the Rule. Or, one can give a power of appointment to a donee to appoint any property which is the subject matter of a challenged interest in such a manner as to approximate the intentions of the person creating the interest. This last method is about the equivalent of the "equitable approximation" method used in *Carter v. Berry*,

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[55]See, *e.g.*, Mass. Gen. Laws Ann. ch. 184A, § 2 (1960); Law of Property Act, 1925, 39 & 40 Geo. 5, c. 98, § 163. See generally Leach, *Perpetuities Legislation, Massachusetts Style*, 67 Harv. L. Rev. 1349 (1954).

[56]See, *e.g.*, Lucas v. Hamm, 56 Cal. 2d 583, 364 P.2d 685 (1961), a recent California case which holds that lack of privity between intended beneficiaries of a will and testator's lawyer does not preclude such intended beneficiaries from bringing an action based on either tort or contract theories for negligently preparing the instrument. However, an attorney is not liable for every mistake he may make and a violation of the Rule is not "[failure] to use such skill, prudence, and diligence as lawyers of ordinary skill and capacity commonly exercise." No liability.

but the one doing the "approximating" is the chosen representative of the testator or settlor, rather than the chancery court.

The following are suggested ideas for "savings clauses":

a. Anything else in this instrument to the contrary notwithstanding, only those beneficiaries who have in fact met the required contingency or condition within 21 years after the death of the survivor of [name a reasonable number of lives in being, including those lives "indicated"[57] by the instrument] shall take.[58]

b. Anything else in this instrument to the contrary notwithstanding, any condition or contingency required for vesting shall be deemed to have been met by any beneficiary (if the condition or contingency could possibly later be met) 21 years after the death of the survivor of [names lives in being].[59]

c. Any interest or interests which fail because of the Rule against Perpetuities or any other like rule is violated shall not go by intestacy but are hereby devised and bequeathed as follows: [Make alternate gift].[60]

d. The Standard Perpetuities Saving Clause drafted by Leach and Logan can be found in 74 Harv. L. Rev. 1141 (1961) and in Leach & Logan, *Future Interests and Estate Planning* 982 (1962). The authors suggest that this clause may be incorporated in the instrument by reference. A disinterested corporate fiduciary is given the power to appoint assets which are the subject matter of challenged interests.[61]

John H. Hogue, Jr.

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[57]See Carter v. Berry, 140 So. 2d 843, 848 (Miss. 1962).

[58]Here, if a contingency has not been met at the end of that period, the interest falls, but not the whole gift. This may seem harsh on one who nearly meets the contingency, but otherwise the interest would have been invalid under the Rule.

[59]Here, all beneficiaries who might later meet the contingency meet it artificially, thanks to the savings clause. Perhaps some will take who would not later have met the contingency, but again the gift is valid by its own terms.

[60]Or one can use a separate like clause for each gift. If the gift is one to a class, specify whether the whole gift is to fall or only such interests as, in themselves, otherwise violate the Rule.

[61]Whether this clause will work as to Mississippi realty rates a query by the drafters. It will help, at least, if the "Donee Statute" is not violated in some manner, and probably will help then. But obviously the same danger applies in Mississippi to any perpetuities savings clause.

THE LIFE INSURANCE TRUST IN ESTATE PLANNING

I. Introduction

One of the most valuable tools of an estate planner is life insurance. It may be used to build or complete an estate. However, the actual distribution of insurance proceeds to fit an estate plan presents a problem. Policy options offered in the insurance contract guarantee certainty, regularity of payment, a fixed rate of interest, and allow use of a $1,000 annual income tax exclusion on interest income to a surviving spouse.[1] However, in some situations options lack the flexibility required for a good estate plan. The life insurance trust, an ordinary trust having an insurance policy as corpus, allows the maximum in flexibility[2] and is gaining in prominence as a means of handling liquid insurance proceeds.

Insurance trusts are defined and classified according to purpose, method of premium payment, and control retained by the settlor. As to purpose, insurance trusts may be personal or business in nature. Business insurance trusts are used to finance commercial transactions and will not be included in this discussion.[3] With relation to premium payment, insurance trusts may be funded or unfunded.[4] In the funded trust arrangement, an insurance policy is transferred to a trust along with income producing securities, the income of which is used to pay premiums on the insurance policy. The unfunded insurance trust consists of the policy or right to proceeds, and premiums must be paid from another source. The settlor may maintain control through the use of a revocable trust, but an irrevocable trust places the corpus beyond the settlor's control.[5] Combinations of the above types of insurance trusts result in different legal and tax consequences.

This paper will analyze the advantages of insurance trusts in two sections. The first section will discuss the non-tax advantages available when a trust is used to distribute insurance proceeds. The second section will be devoted to tax advantages of the insurance trust and suggested methods of obtaining these advantages. A third section will discuss

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[1]Barton, *Life Insurance Planning*, 98 Trusts & Estates 16 (1959); see Int. Rev. Code of 1954, § 101(d) with reference to $1,000 exclusion. See also Shattuck, An Estate Planner's Handbook § 6 (1948); Hawley, *The Use of Life Insurance in Planning Small Estates*, 25 Rocky Mt. L. Rev. 149 (1953).

[2]See Oppenheim, *Life Insurance Trusts in Louisiana*, 32 Tul. L. Rev. 37 (1957); Schwartz, *Life Insurance Estate Planning*, 35 So. Cal. L. Rev. 1 (1961).

[3]For discussion of the business insurance trust, see Shattuck, *op. cit. supra* note 1, § 8; Wolf, *Drafting an Insurance Trust*, 98 Trusts & Estates 997 (1959); 2 Fed. Est. & Gift Tax Rep. § 7263 (1960).

[4]For discussion of funded and unfunded insurance trusts, see Shattuck, *op. cit. supra* note 1, § 7; Doyle, *Life Insurance in Estate Planning*, 22 Ohio St. L.J. 258 (1961); Schwartz, *supra* note 2.

[5]See Doyle, *supra* note 4; Schwartz, *supra* note 2.

creation of the insurance trust and offer suggestions to insure that the trust accomplishes its purpose.

II. Non-Tax Advantages

A. General Advantages

The many inherent advantages of insurance, especially the furnishing of immediate cash at death of the insured, make it readily adaptable to use in a flexible trust arrangement. For instance, an insurance trust can furnish liquidity for the insured's estate.[6] Provision can be made in the trust instrument for giving the trustee discretion to pay death taxes and expenses of the estate with insurance proceeds;[7] and the trustee may be given authority to purchase non-liquid assets from the executor of the insured's estate, thus preventing the necessity of sale at sacrifice prices.[8]

Further illustrating flexibility, the trustee can utilize discretionary authority to invade principal or income for benefit of any beneficiary based upon need or emergency.[9] A minor or otherwise inexperienced beneficiary can be protected from wasting insurance proceeds through unwise investments or loans since a professional trustee will control the proceeds, and the necessity of a formal guardianship, usually required in an option arrangement, is avoided.[10] Secrecy is possible where the insured desires to keep the worth of his estate out of public knowledge.[11]

Use of the trust device permits capital appreciation in the hands of the trustee,[12] thus affording a guard against inflation.[13] In addition, the insurance trust can assure that corpus will be preserved for any remaindermen. For instance, $100,000 of insurance left with an insurer might give a widow 40 years old a life income of $4,000 per year, but at her death both principal and interest probably would have been expended. An insurance trust arrangement would produce more interest than the insurer offers; thus $100,000 would likely produce $4,000 income alone and leave the $100,000 corpus intact.[14] The trust also in-

[6]Wormser, The Planning and Administration of Estates 42 (1961); Schwartz, *supra* note 2.

[7]Barton, *supra* note 1; Oppenheim, *supra* note 2.

[8]Clements, *Insurance Trusts*, 43 Ill. B.J. 336 (1955); see Note, 12 N.Y.U. Intra. L. Rev. 93 (1957).

[9]See Oppenheim, *supra* note 2; Schwartz, *supra* note 2. See also Barton, *supra* note 1.

[10]*Ibid.*

[11]Doyle, *supra* note 4; Schenck, *The "Pour-Over" Technique in Estate Planning*, 38 Taxes 57 (1960); Stephens & Johnson, *Life Insurance in Estate Planning*, 15 Sw. L.J. 570 (1961).

[12]Barton, *supra* note. 1.

[13]Wormser, *op. cit. supra* note 6, at 57; Doyle *supra* note 4.

[14]Moore, *Insurance Aspects of Estate Planning*, 95 Trusts & Estates 616 (1956); Oppenheim, *supra* note 2.

sures continuity of management of funds after death of the life beneficiary.[15]

A properly constructed insurance trust can protect against insolvency and financial loss of the insured, and proceeds payable to an inter vivos life insurance trust usually cannot be reached by creditors of the insured or creditors of the beneficiary if a spendthrift trust is utilized.[16] Use of a trust also avoids will contests over undue influence or the like,[17] and renunciation by the wife.[18] Naturally the trust will allow a more complex plan of distribution than the option system, and there will be unified handling of the proceeds of policies from several different companies.[19]

In comparison to an option selection, the insurance trust has few disadvantages. Use of the trust device results in loss of an annual income tax exclusion of $1,000 on interest income available to a surviving spouse under option arrangements;[20] and unlike the option plan, a trust will require some administration expense. However, the desire for flexibility and other advantages of the insurance trust far outweigh any disadvantages.

B. "Pour-Over" from a Will to an Insurance Trust

One of the more useful advantages is that utilization of the insurance trust makes it possible to merge other assets with life insurance proceeds and administer the aggregate as one fund.[21] For example, pension, profit sharing and stock bonus plans can be deposited in an insurance trust.[22] Lifetime transfers of assets can be made to the insurance trust and/or a will can be written to "pour-over" assets into an inter vivos insurance trust resulting in their being administered by the terms of the trust.[23] These "pour-over" assets would escape probate supervision,[24] and swelling of the estate would be avoided, thereby saving

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[15]Barton, *supra* note 1.

[16]Schwartz, *supra* note 2; see Leigh v. Harrison, 69 Miss. 923, 11 So. 604 (1892), for recognition of spendthrift trust in Mississippi; Miss. Code Ann. § 308 (1956) which exempts $10,000 of proceeds paid to any beneficiary from insured's debts. See also Nossaman, 1 Trust Administration & Taxation § 14.02 (2d ed. 1961) for discussion of rights of creditors against trust consisting of life insurance proceeds.

[17]Schwartz, *supra* note 2.

[18]See Beatty, *Insurance Proceeds in Trust*, 28 Tenn. L. Rev. 344 (1961).

[19]See Barton, *supra* note 1; Clements, *supra* note 8; Oppenheim, *supra* note 2; Schwartz, *supra* note 2.

[20]See Int. Rev. Code of 1954, § 101(d) which mentions exclusion only as to amounts held by insurer.

[21]See Barton, *supra* note 1.

[22]Schwartz, *supra* note 2.

[23]See Miss. Code Ann. § 661.5 (Supp. 1960) which establishes the validity of the "pour-over" provision in Mississippi.

[24]See Wormser, *op. cit. supra* note 6, at 32; Doyle, *supra* note 4.

estate administration expenses.[25] By proper provision "pour-over" can be made to an insurance trust created in another state where laws are more favorable to the decedent's purposes.[26]

In the absence of a specific statute, "pour-over" into an inter vivos trust has been supported by the doctrine of incorporation into the will by reference or the doctrine of independent significance.[27] Professor Casner notes that the doctrine of incorporation by reference is satisfied if the trust instrument is in existence when the will is executed. If state law requires the trust to be in existence at the execution of the will in order to satisfy the doctrine, a nominal sum may be placed in the trust as corpus and removed when a policy is made payable to the trustee.[28] In most instances there should be no problem in upholding a "pour-over" provision in a state where incorporation by reference is accepted if the trust agreement is in existence at execution of the will.

An increasing number of states have adopted statutes expressly providing for use of a "pour-over" provision. Wisconsin has such a statute which provides that a valid inter vivos trust created by a written instrument can receive property bequeathed or devised under a will, and that reference to the trust in the will does not cause trust assets to be administered as a part of the decedent's estate; however, if the trust is amended after execution of the will, the amendment will not be effective as to property passing under the will unless the will is republished or executed after the amendment.[29] The statute also provides that an insurance policy is a sufficient trust res.

Mississippi has a very liberal "pour-over" statute.[30] One can devise to any trust evidenced by a written instrument in existence and identified in the will. The devise is not invalid because the trust is amendable or revocable. The liberal portion of the Mississippi statute is the provision that if the trust is amended after execution of the will, property devised to the trust under the will passes under the amendment automatically. In effect, the testator by amending the trust can change the disposition of "pour-over" property without having to republish his will. The property "poured-over" will not be deemed held under a testamentary trust. Other states have similar statutes.[31]

It is recommended that the estate planner inform his client of the

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[25]Doyle, *supra* note 4; Schenck, *supra* note 11.

[26]See WORMSER, *op. cit. supra* note 6, at 32, 288; Schwartz, *supra* note 2.

[27]See State *ex rel.* Citizen's Nat'l Bank v. Superior Court, 236 Ind. 135, 138 N.E.2d 900 (1956); RESTATEMENT (SECOND), TRUSTS § 54(1) (1959); Annot., 80 A.L.R. 103 (1932).

[28]CASNER, ESTATE PLANNING 283 (3d ed. 1961).

[29]WIS. STAT. ANN. §§ 206.52, 253.03(1), 323.01 (1957); see 1956 WIS. L. REV. 313.

[30]MISS. CODE ANN. § 661.5 (Supp. 1960).

[31]*E.g.*, PA. STAT. ANN. tit. 20, § 180.141 (1950); see WORMSER, *op. cit. supra* note 6, at 287.

effect of a trust amendment upon the will at the time the will is executed. In the absence of an express statute like that in Mississippi, an amendment to the trust should be followed immediately by republishing of the will or execution of a new will. The estate planner also must warn his client that disastrous results can occur when the settlor moves from the state where the trust and "pour-over" will were executed and subsequently dies in another state without having checked the status of his estate in the new jurisdiction.[32]

III. Tax Advantages of Insurance Trusts

A. Introduction

Some of the chief advantages of insurance trusts are found in the tax field. Since this field is highly technical and complicated, a simple enumeration of advantages is useless unless accompanied by illustrations showing how these advantages are achieved. This discussion will illustrate methods of obtaining tax advantages and will indicate pitfalls that should be avoided in the tax area.

Since most tax advantages can be obtained only through use of an irrevocable trust, this type trust will be the main subject of discussion. To possess tax advantages, the grantor must release completely his ownership and control of the policy and any funded securities. Thus, the irrevocable trust should appeal to a grantor who desires to save on taxes and expects no financial problems which would result in a need for the insurance policy or funded securities.

B. Irrevocable Trusts

1. *Gift Tax Advantages*

a. *General*

A gift of an insurance policy is complete and subject to the gift tax if the grantor has no reversionary interest, no power to vest economic benefits or proceeds in himself or his estate, and no power to change beneficiaries.[33] Thus, assignment of a policy and funding securities to an irrevocable trust without consideration constitutes a gift.[34] Consequently, in most cases one can reduce his estate and pay less tax, since the gift tax rate is lower than the estate tax rate. The donor must remember, however, that he is liable for any gift tax and that if he fails to pay the tax, the beneficiary will be liable.[35]

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[32]See Wolf, *supra* note 3.

[33]See Treas. Reg. § 2511-1 (h) (8) (1958); Erbacher, *Life Insurance and Gift Tax*, 93 Trusts & Estates 616 (1954) for discussion of gift tax problems.

[34]See Int. Rev. Code of 1954, § 2511 (a); Wolf, *supra* note 3. *But see* Fletcher Trust Co. v. Commissioner, 141 F.2d 36 (7th Cir. 1944).

[35]Int. Rev. Code of 1954, § 6324 (b).

The method of valuation of a gift of insurance affords a sizeable tax advantage. The gift tax will be computed on the value of the policy on the date of the gift and not its greatly increased value at death of the insured.[36] If the policy subject to the gift is a single premium policy, its value is the cost to the donor.[37] Where the policy transferred to the trust requires further payment of premiums, its value is the replacement value of the policy. This amount is computed ". . . by adding to the interpolated terminal reserve at the date of the gift the proportionate part of the gross premium last paid before the date of the gift which covers the period extending beyond that date."[38] The value of the terminal reserve can be obtained from the insurance company.

If the policy has a small terminal reserve and if the annual exclusion or specific exemption is available, there may be no gift tax. If the gift qualifies for the $3,000 annual exclusion, this amount can be deducted from the value of the gift.[39] In addition, if the lifetime specific exemption is available, another $30,000 can be deducted from the value of the policy, thereby further reducing the gift tax due.[40]

b. *Qualifying for the Annual Exclusion*

If the policy premiums in an unfunded irrevocable trust are paid by the grantor or a third person, a gift is complete at the time of payment;[41] but generally the annual exclusion is not available since the gift is a future interest.[42] In order to qualify for the gift tax annual exclusion, a transfer must be a gift of a present interest, and "An unrestricted right to the immediate use, possession, or enjoyment of property or the income from property is a present interest in property."[43] In qualifying for the annual exclusion, flexibility is diminished. Consequently, the annual exclusion is not usually available because the insured grantor will not desire that his beneficiaries have the right to immediate possession since a primary purpose for using the trust device was to avoid immediate possession.[44]

If the annual exclusion is desired despite loss of flexibility, the insured can make an outright and unqualified gift by assignment of the policy to an unfunded trust with the beneficiary having the unrestricted right to demand immediate possession and exercise all incidents of ownership. Lack of cash value is no indication that the policy is a gift of

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[36] INT. REV. CODE OF 1954, § 2512 (a).

[37] Guggenheim v. Rasquin, 312 U.S. 254 (1941).

[38] See Treas. Reg. § 25.2512-6 (1958); Goodman v. Commissioner, 156 F.2d 218 (2d Cir. 1946).

[39] INT. REV. CODE OF 1954, § 2503 (b).

[40] INT. REV. CODE OF 1954, § 2521.

[41] See INT. REV. CODE OF 1954, § 2511; Treas. Reg. § 25. 2511-1 (h) (8) (1958).

[42] See INT. REV. CODE OF 1954, § 2503 (b).

[43] Treas. Reg. § 25.2503-3 (b) (1958).

[44] See Schwartz, *supra* note 2; Wolf, *supra* note 3.

a future interest.[45] If the insured continues to pay the premiums, the annual exclusion is available.[46] If the beneficiaries cannot obtain the income until they reach a certain age, there is insufficient present interest even though the trustee may expend for health of the beneficiaries.[47] A sufficient present interest should exist if the beneficiaries are entitled to demand trust property from the date the trust was created.[48] If the insurance policy is fully paid up but dividends or interest only is payable to the beneficiary, there is a present interest as to the dividends and a future interest as to the proceeds.[49]

The Code makes specific provisions for qualifying a gift to a minor for the annual exclusion.[50] "An unqualified and unrestricted gift to a minor with or without the appointment of a legal guardian is a gift of a present interest; and disabilities placed upon minors by state statutes should not be considered decisive in determining whether such donees have the immediate enjoyment of the property or the income therefrom within purport of the Federal gift tax law."[51] However, state law should be adhered to so that the trust instrument itself will be valid. As a word of caution, the estate planner should avoid giving two children joint power to demand the policy from the trustee. Since joint, unanimous action of the donees is required to obtain the policy, the gift may be a future interest.[52]

It should be remembered that under the split gift provision a husband joined by his wife can give away $6,000 tax free to a trust for payment of premiums provided a present interest exists.[53] Another important point to remember is that the $30,000 specific exemption applies to gifts of both present and future interests and together a husband and wife can give away $60,000.[54] Thus, if the insured has not used his specific exemption, he may transfer the policy or funding securities tax free without losing flexibility by qualifying the trust for the annual exclusion.

c. *Gift Tax Marital Deduction Trust*

If rigid Code requirements are met, 50 percent of the value of a gift of insurance in trust may pass to the wife tax free under the marital

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[45]Rev. Rul. 55-408, 1955-1 Cum. Bull. 113.

[46]Treas. Reg. § 25:2503-3 (c) -6 (1958).

[47]See Francis F. Bolton, 1 T.C. 717 (1943). See also Jesse S. Phillips, 12 T.C. 216 (1949).

[48]See Harbeck v. Halsted, 28 T.C. 1069 (1957), *acq.*, 1958-1 Cum. Bull. 5.

[49]See Pauline Wilkens Tidemann, 1 T.C. 968, *acq.*, 1943 Cum. Bull. 23.

[50]Int. Rev. Code of 1954, § 2503 (c).

[51]Rev. Rul. 54-400, 1954 Cum. Bull. 319.

[52]See Skouras v. Commissioner, 188 F.2d 831 (2d Cir. 1951); Burford, *Insurance Owned by Wife on Husband*, 100 Trusts & Estates 1014 (1961).

[53]See Int. Rev. Code of 1954, § 2513; Treas. Reg. § 25.2513-2 (1958).

[54]Int. Rev. Code of 1954, § 2521; Treas. Reg. § 2521-1 (b) (1958).

deduction provision. To qualify a gift of life insurance in trust for the marital deduction, the following conditions must be met: (1) The wife must be entitled to all income from the entire interest or a specific portion thereof, payable annually or at more frequent intervals. (2) The donee spouse must have the power exercisable alone and in all events to appoint her interest to herself or her estate. (3) There must be no power in anyone else to appoint any part of such interest to anyone other than the donee spouse.[55] If the policy transferred by the husband is unproductive, the wife must have the power to compel the trustee to convert the property to income producing property or she must be able to terminate the trust and demand the policy.[56] This tax saving device should not be overlooked in disposing of insurance policies.

2. *Income Tax Effect on the Funded Trust*

Obtaining income tax advantages is important when an irrevocable trust is to be funded. At first glance it appears that there are no income tax advantages in creating an irrevocable funded life insurance trust. If the insured grantor funds any life insurance trust with income producing securities, the income of which is or may be used to pay premiums on the insurance policy covering his life without the consent or approval of an adverse party, this trust income is taxable to the grantor.[57] If the trustee has the discretion to pay premiums but does not do so, this income is taxable to the grantor as it could have been used to pay premiums.[58] The insured cannot escape this result by furnishing another person with funds to establish an insurance trust as the insured will be considered the grantor.[59] However, it has been held that the grantor will not be taxed on excess income unnecessary for premium payment.[60]

The grantor can avoid being taxed on trust income if he is willing to provide in the trust agreement that the income may be used to pay premiums provided a designated beneficiary does not demand the income. This procedure would seem to meet the requirements of the Code as the income could be used to pay premiums only with the consent of an adverse party.[61] An adverse party is ". . . any person having a substantial beneficial interest in the trust which would be adversely affected by the exercise or non-exercise of the power which he possesses

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[55]INT. REV. CODE OF 1954, § 2523 (e).

[56]Treas. Reg. § 25.2523 (e)-1 (f) (4), (6) (1958).

[57]INT. REV. CODE OF 1954, § 677 (a); see Burnet v. Wells, 289 U.S. 670 (1933), upholding constitutionality of Code provision.

[58]Arthur Stockstrom, 3 T.C. 664 (1944); see Rieck v. Commissioner, 118 F.2d 110 (3d Cir. 1941).

[59]Lorenz Iversen, 3 T.C. 756 (1944).

[60]Joseph Weil, 3 T.C. 579 (1944).

[61]See INT. REV. CODE OF 1954, § 677 (a).

respecting the trust."[62] Undoubtedly, the beneficiary having power to demand the income would possess sufficient adverse interest. The beneficiary would then be taxed on the income by virtue of his power to demand that it be paid to him.[63]

An illustration of how such an arrangement could work is the case where a grandfather wishes to provide for his grandchildren. He could purchase an insurance policy on his life and establish an irrevocable funded life insurance trust with the proceeds to be held solely for his grandchildren. By providing that income of the trust would be used to pay premiums unless his son demanded the income, the grandfather should escape income tax. Of course, if the son was in a high income bracket, this procedure would not be practical as the son would be taxed on the income.[64]

Variations of the above arrangement have also been expounded. The son can be given power to require that the income be distributed to him currently or accumulated for him with the trustee having the ultimate power to determine whether it will be accumulated or distributed. Income used to pay premiums probably would not be taxed to either the grandfather or to the son but rather to the trust since the power is not exercisable solely by the son,[65] and the Code makes an exception to holding the grantor owner of income temporarily withheld.[66] If the trustee accumulates the income, it should be taxable to the trust.[67] The existing laws on accumulations of income must be observed.

Another variation would be to give the son power to require the trustee to distribute income to any one or more of a class composed of the son and the son's issue with the trustee having the power to determine who would receive the income. Income used to pay premiums should not be taxable to the father or to the son but to the trust as outlined above. However, income would be taxable to those beneficiaries receiving income in the trustee's discretion.[68]

The son might be considered as having made a gift to the beneficiaries in the first two illustrations above. However, there is a $5,000 exclusion applicable to the lapse of a general power of appointment in any year, so realistically speaking there should be no gift unless over $5,000 of income is available.[69] For the above arrangements to withstand the scrutiny of the tax service, the grandfather must be absolutely

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[62] INT. REV. CODE OF 1954, § 672 (a).

[63] INT. REV. CODE OF 1954, § 678 (a) (1).

[64] See Mannheimer, Wheeler, Friedman, *An Unexplored Form of Insurance Trust*, 34 TAXES 494 (1956), for excellent discussion of this arrangement.

[65] INT. REV. CODE OF 1954, § 678 (a) (1).

[66] INT. REV. CODE OF 1954, § 674 (b) (6).

[67] See Mannheimer, *supra* note 64.

[68] See INT. REV. CODE OF 1954, § 662; Mannheimer, *supra* note 64.

[69] INT. REV. CODE OF 1954, § 2514 (e).

willing for the son to control the income, and there must be no agreement concerning the matter between father and son.

Two donors can join in creating a funded irrevocable trust and obtain income tax advantages. The insured husband can contribute policies on his life to the trust, paying a gift tax on the present value of the policies. His wife may then transfer her separate income producing securities to the trust, paying a gift tax and designating that the income be used to pay premiums on her husband's insurance policies. If the wife is not a beneficiary under the trust and neither husband or wife reserves any rights in the trust, the income will be taxed to the trust and not to the wife since the policies cover her husband's life.[70] However, if the wife is a beneficiary, the income will be taxed to her since it is held or accumulated for her benefit without the approval of any adverse party.[71] For instance, a husband contributed policies on his life and his wife transferred 1,000 shares of income producing stock, the income of which was to be used to pay premiums. The wife was to receive $800.00 per month out of proceeds at her husband's death. The court held that the income of the trust was taxable to the wife because, in effect, it was accumulated for future distribution to her, the grantor. The fact that she had to survive to receive any amount was of no consequence.[72] To avoid this result, the funding grantor must not be named beneficiary of the trust. The two donor type irrevocable trust is extremely useful and allows husband and wife to work directly together in planning distribution of their wealth and providing for their loved ones.

If the grantor creates an irrevocable insurance trust with any income therefrom going to the beneficiary and the beneficiary voluntarily pays premiums on the insurance policy covering the grantor's life, the income is not taxable to the grantor since the income belongs to the beneficiary.[73] Any understanding or direction that income will be used to pay premiums will result in the grantor being taxed on income so used.[74] If a husband gives his wife securities and life insurance policies and she later voluntarily transfers them to a trust and obligates the trust to pay the premiums, the husband will not be taxed on the income.[75] However, such arrangements will be carefully scrutinized and will fail unless absolutely voluntary in nature.

Another possible way to avoid income tax on an irrevocable funded trust is to specify that income will be paid to a beneficiary with principal being used to pay premiums as the Code does not specifically men-

[70]See INT. REV. CODE OF 1954, § 677 (a) (3).
[71]See INT. REV. CODE OF 1954, §§ 677 (a) (2), 673.
[72]Edward H. Wadewitz, 32 T.C. 538 (1959).
[73]George F. Booth, 3 T.C. 605 (1944).
[74]See L. B. Foster, 8 T.C. 197 (1947).
[75]Rockwell v. Granger, 62 F. Supp. 907 (W.D. Pa. 1945).

tion use of principal to pay premiums.[76] Other arrangements discussed above obviously have more merit than this method because principal is not expended. It should be noted that one can fund an insurance trust consisting of policies on his life and escape income tax on income used to pay premiums if the proceeds are irrevocably payable to a charity.[77]

The short term funded trust affords an excellent means for one to fund an insurance trust on the life of another person, avoid income tax, and get all the funded securities back. The income of a funded insurance trust is taxable to the grantor if trust property or income will or is reasonably expected to revert to the grantor within ten years.[78] Thus a father could purchase a policy covering his son's life, set up an irrevocable insurance trust and fund it for over ten years, retaining a reversion of the funded securities. Provided the trust or the beneficiary owned the policy, the father would not be taxed on income from the securities used to pay premiums. In effect, the securities "lent" to the trust would build a valuable asset for the son at no cost to the father. The income would be taxed to the trust or beneficiary depending upon who owned the policy.

Several precautions must be observed in funding a trust and avoiding income tax. One such precaution is ascertaining applicable state law before formulating the trust agreement. For example, the Code indicates that if the trust beneficiary is one whom the grantor is under a legal duty to support, the income will be taxable to the grantor to the extent so used.[79] However, in a case which seems to disregard the present Code, a husband transferred non-income producing insurance policies to a trust for his children, and the wife contributed income producing property. There was no requirement that income be used to pay premiums, but it was so used. The court looked to both the statutes and judicial decisions of Tennessee and despite the wording of the Code, held the income taxable to the wife because it could have been used to discharge her legal obligation under state law to support her children in the discretion of trustees having no substantial adverse interest.[80]

The income will also be taxable to the grantor if the beneficial enjoyment can be determined by the grantor and a non-adverse party.[81] In addition, retention of certain administrative powers over the trust will result in the grantor's being taxed on income;[82] and if the grantor

[76]See INT. REV. CODE OF 1954 § 677 (a); Bennett v. United States, 185 F. Supp. 577 (N.D. Ill. 1960).

[77]See INT. REV. CODE OF 1954, § 677 (a) (3); TWEED & PARSONS, ABA-ALI LIFETIME AND TESTAMENTARY ESTATE PLANNING 46, 68; Comment, 33 MISS. L.J. 381 (1962).

[78]INT. REV. CODE OF 1954, § 673.

[79]INT. REV. CODE OF 1954, § 677 (b).

[80]See W. C. Cartinhour, 3 T.C. 482 (1944).

[81]INT. REV. CODE OF 1954, § 674.

[82]INT. REV. CODE OF 1954, § 675.

may revoke the trust without consent of an adverse party, the income will be taxable to him.[83]

3. *Estate Tax Advantages*

a. *General*

It is often an advantage to keep insurance proceeds out of the grantor's gross estate by making a gift or transferring the policy for consideration while its value is small in comparison to its greatly increased value at death. If the estate is already sizeable, the addition of insurance proceeds at death will enlarge the estate subject to tax. Consequently, the grantor can reduce his gross estate and save estate taxes by transferring the policy and any funding securities to an irrevocable insurance trust.

Assignment of an insurance policy to an irrevocable trust can produce an estate tax saving if several requirements are met. The first requirement dictates that sections 2036 through 2038 of the Code must be followed explicitly in formulating the trust agreement. If the grantor retains any right to the trust income, the property producing this income will be included in his gross estate.[84] A power in the grantor to alter, amend, revoke, or terminate the trust will also result in inclusion of the trust property.[85]

The second requirement concerns the transfer of the policy to the trust and necessitates a careful review of section 2042 of the Code which establishes the incidents of ownership test. If the insured retains any incident of ownership in the policy arising out of the trust or the policy, the proceeds will be included in his gross estate.[86] Some common incidents of ownership are the power to change the beneficiary, power to obtain cash or loan value, power to surrender or cancel the policy, right to borrow on the policy without consent of a beneficiary, and power to change the time and manner of enjoyment of proceeds.[87]

Section 2042 of the Code also provides that a reversionary interest in the policy exceeding five percent of the value of the policy immediately before the death of the decedent is an incident of ownership regardless of how the reversion arises. Accidental reversions may result from a violation of the Rule against Perpetuities and failure to provide for the situation where all beneficiaries die before the insured. The latter cause of reversion can be eliminated by naming sufficient contingent beneficiaries. Another suggestion that has been offered for avoiding a

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[83]INT. REV. CODE OF 1954, § 676.

[84]INT. REV. CODE OF 1954, § 2036.

[85]INT. REV. CODE OF 1954, § 2038.

[86]INT. REV. CODE OF 1954, § 2042 (2).

[87]See Treas. Reg. § 20.2042-1 (c) (4) (1958); Schwartz, *Life Insurance Estate Planning*, 35 So. CAL. L. REV. 1 (1961).

reversion is to have the grantor establish an irrevocable trust and let the trustee purchase the insurance.[88]

A provision requiring the trustee to pay debts, taxes, or enforceable obligations against the estate will be treated as an incident of ownership, and the amounts required for payment will be included in the gross estate.[89] However, if the trustee's power is discretionary and the trust is for named individuals, proceeds are taxable in the estate only to the extent so used.[90] The right of a beneficiary to consent to a policy change has been held an incident of ownership although the beneficiary had no power to initiate change; thus, the term "incident of ownership" is not limited to ownership in a technical legal sense.[91] State law can also indicate incidents of ownership and should be checked.[92]

Not every retained power is an incident of ownership. It has been held that neither the right to direct trust investments in a funded trust[93] nor the right to receive policy dividends is an incident of ownership.[94] This latter result probably was reached because dividends often are considered a return of premiums previously paid. As a precaution, it would be best not to retain these powers.

The third requirement is that the transfer must not be made in contemplation of death. If the insured-grantor dies within three years after transferring the policy to the trust, the transfer is presumed to have been made in contemplation of death and included in the gross estate unless the presumption is rebutted by showing a life motive.[95] There is a conflict of authority as to what happens when one pays premiums on an insurance policy within three years of death. The amount included in the gross estate may be the actual cash amount of premiums paid during the three years, a proportionate share of the face value of the policy determined by premiums paid within three years, or the full value of the insurance.[96] Some authorities feel that a proportion of the proceeds should be included,[97] and this result appears to be fair. To avoid this situation, it might be wise to have the beneficiary or assignee pay the premiums for the first three years after transfer to the trust.[98]

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[88]See Clements, *Insurance Trusts*, 43 ILL. B.J. 336 (1955).

[89]Treas. Reg. § 20.2042-1 (b) (1) (1958).

[90]See Estate of Charles Howard Wade, 47 B.T.A. 21 (1942).

[91]See Commissioner v. Karagheusian's Estate, 233 F.2d 197 (2d Cir. 1956).

[92]Treas. Reg. § 20.2042-1 (c) (5) (1958).

[93]Estate of Edmund W. Mudge, 27 T.C. 188 (1956), *acq.*, 1957-1 CUM. BULL. 4.

[94]Estate of Chester H. Bowers, 23 T.C. 917 (1955), *acq.*, 1955-2 CUM. BULL. 4.

[95]INT. REV. CODE OF 1954, § 2035; see NOSSAMAN, TRUST ADMINISTRATION AND TAXATION § 38.22 (2d ed. 1961); Wolf, *Drafting an Insurance Trust*, 98 TRUSTS & ESTATES 997 (1957).

[96]See Burford, *supra* note 52.

[97]See Wolf, *supra* note 95.

[98]See Dicus, *Some Implications of the 1954 Code for Estate Planning*, 32 TAXES 938 (1954).

b. *Powers of Appointment*

Through utilization of a power of appointment the grantor can control the application of estate tax on the interests of beneficiaries to the trust. A general power of appointment exists where one has the power to appoint property to himself, his estate, his creditors, or the creditors of his estate; the property subject to the power will be taxed to the possessor regardless of whether the power is exercised.[99] Thus if the grantor gives any beneficiary a general power of appointment, an estate tax will be collected at the beneficiary's death.

Any power not within the definition of a general power is a special power and entails no tax consequences. If the insured-grantor does not desire that the beneficiary control final disposition of the property, he can give him a special power to appoint according to the individual needs of a class designated by the insured. This procedure allows the grantor to provide for flexibility even after his death and at the same time skip a generation of beneficiaries in application of the estate tax. Thus, proper use of powers of appointment given to insurance trust beneficiaries offers many advantages.

c. *Estate Tax Marital Deduction Trust*

The insurance trust can also be utilized to obtain an estate tax marital deduction allowing 50 percent of the adjusted gross estate to pass to the wife tax free. The intricacies of the marital deduction trust are too broad for a detailed discussion in this paper, and only a sketch can be presented in this section.[100]

To qualify a life insurance trust for the estate tax marital deduction, practically the same requirements outlined for the gift tax marital deduction must be followed. The interest must pass from the decedent to the surviving spouse and payments must begin within thirteen months of death of the insured.[101] The husband can name contingent beneficiaries who will take in case the wife fails to exercise her general power of appointment, and this will not disqualify the trust.[102] The wife's power must be exercisable in all events, and the estate planner also should examine the policy itself to insure that this result will follow.[103]

The maximum marital deduction allowable is usually desired, and a "pour-over" provision affords a means of maximizing the marital deduction. A trust qualifying for the marital deduction and a non-marital

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[99]INT. REV. CODE OF 1954, § 2041.

[100]See Comment, 33 MISS. L.J. 232 (1962), for details on the marital deduction trust.

[101]INT. REV. CODE OF 1954, § 2056(b)(6); Treas. Reg. § 20.2056(b)(6) (1958); Comment, 33 MISS. L.J. 232 (1962).

[102]See Treas. Reg. § 20.2056(b)-6(e) (1958).

[103]Estate of Werbe v. United States, 273 F.2d 201 (7th Cir. 1959).

deduction trust can be established with each trust receiving one-half the insurance proceeds. If "pour-over" is made to both trusts equally, one can maximize the marital deduction.[104]

There are ways to save on taxes and at the same time increase the amount passing to the wife tax-free. For instance, one can set up a revocable or an irrevocable insurance trust for the benefit of a charity, retaining an incident of ownership in the policy. At the insured's death, the value of the policy would be included in his gross estate since he retained the incident of ownership. The marital deduction is figured on the adjusted gross estate which would include this amount going to charity.[105] However, the amount passing to charity would be deducted in determining the taxable estate.[106] By way of illustration, if the husband has an adjusted gross estate of $300,000, he can give $150,000 to his wife tax free. Subtracting the $60,000 exemption, his taxable estate is $90,000 and the tax payable would be $17,500. If the husband took out $100,000 of insurance and placed it in trust for a charity, retaining an incident of ownership, his adjusted gross estate would be $400,000 of which $200,000 would go to the wife tax free under the marital deduction provision. Subtracting the $100,000 payable to the charity and the $60,000 exemption, the net taxable estate would be $40,000 and the tax payable only $4,800.[107] It might even be possible to arrange a similar plan allowing an income tax deduction.

B. Revocable Insurance Trusts

A revocable life insurance trust, whether funded or unfunded, offers no tax advantages or disadvantages to the grantor as compared with his outright ownership of the policy during life.[108] There is no taxable gift in the transfer of the policy to the trust or in the transfer of property to fund the trust as the gift is not complete since the beneficiary may be changed or the trust revoked.[109] If the trust is funded, the grantor, whether or not he is the insured, remains subject to tax on income from the securities.[110] At the grantor's death, the proceeds will

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[104]See Schenck, *The "Pour-over" Technique in Estate Planning*, 38 TAXES 57 (1960).

[105]See INT. REV. CODE OF 1954, § 2056.

[106]INT. REV. CODE OF 1954, § 2055.

[107]See Goldberg, *Funding a Charitable Program with Life Insurance*, 99 TRUSTS & ESTATES 788 (1960), for discussion of this arrangement.

[108]See Doyle, *Life Insurance in Estate Planning*, 22 OHIO ST. L.J. 258 (1961); Schwartz, *supra* note 87. See also SHATTUCK, AN ESTATE PLANNER'S HANDBOOK § 7 (1948).

[109]Treas. Reg. § 25.2511-2(c) (1958).

[110]INT. REV. CODE OF 1954, § 676.

be includible in his gross estate because he possesses incidents of ownership in the policy[111] and the trust is revocable.[112]

The revocable trust is still a useful and valuable device although it does not have the tax advantages afforded by the irrevocable trust. All the non-tax advantages of insurance trusts discussed earlier are applicable and some tax advantages are available to the beneficiaries. By setting up a revocable insurance trust for the life of a beneficiary with the remainder over to another person, the second estate tax can be avoided,[113] and the proceeds will be exempt from income tax in the hands of the beneficiary.[114] The revocable trust may permit selection of state law governing administration of the property.[115] Since the grantor still has control of the policy and may regain its benefits, a revocable trust should always be employed in any case where the grantor's financial needs for the future are uncertain.

Use of the revocable trust requires constant awareness of the gift tax in the situation where the wife or a third person sets up a revocable insurance trust with the husband being the insured and the children the beneficiaries. At the death of the insured, the trust becomes irrevocable and the grantor will be deemed to have made a gift to the beneficiaries. *Goodman v. Comm'r* illustrates these disastrous consequences[116] and should serve as a warning to the estate planner. In *Goodman*, the wife took out insurance on the life of her husband and then set up a revocable insurance trust, naming their children as beneficiaries and retaining incidents of ownership. At the husband's death, the Commissioner alleged there was a gift tax due on the face value of the policies which was around $500,000. The wife argued that the value of the gift was the amount of the premium she had paid which was about $100,000. The court agreed with the Commissioner, and the wife was held liable for a gift tax on nearly $400,000. A possible way to avoid a similar result would be to give the wife a testamentary power to change the interests of the beneficiaries and then provide that the trust would become irrevocable if the husband predeceased the wife.[117]

IV. Creation of the Insurance Trust

A. Manner of Establishment

The owner of an insurance policy is entitled to establish the trust.

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111 Int. Rev. Code of 1954, § 2042 (2).

112 Int. Rev. Code of 1954, § 2038.

113 Schwartz, *supra* note 87.

114 Int. Rev. Code of 1954, § 101 (a).

115 Tweed, *op. cit. supra* note 77, at 43. *But see* Miss. Code Ann. § 467 (1956) which applies in case of intestacy.

116 156 F.2d 218 (2d Cir. 1946).

117 See Treas. Reg. § 25.2511-2 (c) (1958); Burford, *Insurance Owned by Wife on Husband*, 100 Trusts & Estates 1014 (1961).

The owner may be the insured, a beneficiary, or the purchaser of the policy. The trust can be established by agreement between the owner and the beneficiary,[118] or a beneficiary can create a trust by either assigning his rights to another as trustee or declaring himself trustee of his rights under the policy.[119] Some jurisdictions might question the validity of a revocably appointed beneficiary establishing a trust of his interest,[120] but where the beneficiary is irrevocably appointed and has received an assignment of the policies, there should be no question of validity.[121]

Two separate requirements must be met to establish the trust. There must be a trust agreement and a transfer to this trust of an insurance policy constituting the res of the trust. The trust agreement may be a formal express document drawn up separately or incorporated in the policy itself.[122] Failure of a trust to arise due to a faulty trust agreement can wreck an estate plan. If a policy is payable to a person as trustee but no beneficiary can be ascertained on the death of the insured, there is a resulting trust for the estate of the insured.[123] An endorsement on a policy directing the insurer to pay a certain person as trustee without specifying the trustee's duties has resulted in a dry trust with the proceeds going directly to the intended beneficiary.[124] These results obviously were not intended and illustrate the necessity of having a thorough and complete written agreement.

There is a conflict of authority on whether a beneficiary can keep proceeds payable directly to him under circumstances where he did not know of a previously executed instrument directing him to pay over to another. Some cases have held that no trust could be created without the beneficiary's knowledge of the desired trust even though the instrument directing the beneficiary to pay over part of the proceeds was witnessed.[125] Other cases illustrate that courts will find a trust even though the beneficiary had no knowledge of the intended trust or of the fact that he was a beneficiary.[126] Consequently, the insured grantor

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[118]See SCOTT, TRUSTS §§ 57.3, 84.1 (2d ed. 1956); BOGERT, 1A TRUSTS AND TRUSTEES § 142 (a) (1951); RESTATEMENT (SECOND), TRUSTS § 84, comment b (1959).

[119]*Ibid.*

[120]*But see* RESTATEMENT (SECOND), TRUSTS § 84, comment b (1959), which states that the rights of the beneficiary may be held in trust although the insured has reserved power to change beneficiary.

[121]See First Trust Co. v. Northwestern Mut. Life Ins. Co., 204 Minn. 244, 283 N.W. 236 (1939).

[122]RESTATEMENT (SECOND), TRUSTS § 57.3 (2d ed. 1956).

[123]Seran v. Davis, 174 Okla. 433, 50 P.2d 662 (1935); SCOTT, TRUSTS § 57.3 (2d ed. 1956); see National Bank v. Savarika, 167 Miss. 571, 148 So. 649 (1933).

[124]Bellinger v. Bellinger, 180 Misc. 948, 46 N.Y.S.2d 263 (Sup. Ct. 1943).

[125]*E.g.*, Union Cent. Life Ins. Co. v. Mac Briar, 66 Ohio App. 144, 31 N.E.2d 172 (1940).

[126]*E.g.*, Carter v. Carter, 321 Pa. 391, 184 Atl. 78 (1936); see Ballard v. Ballard, 296 S.W.2d 811 (Tex. Civ. App. 1956).

would be acting unwisely if he attempted to establish a trust without informing the intended beneficiary of the trust arrangement.

The second requirement for establishing the trust, the transfer of the insurance policy to the trust, may be accomplished in two ways: (1) by assignment and (2) by change of beneficiary. An assignment of the policy to a beneficiary as trustee followed by proper notice divests the owner of all his rights in the policy. Thus, assignment should be used when the insured desires to divest himself of all incidents of ownership and establish an irrevocable trust. However, a formal assignment is not essential for having a valid trust.[127] The other method of transfer is simple and involves changing the beneficiary to the trustee in a presently existing policy or naming the trustee as beneficiary in a new policy. The change of beneficiary method does not divest the insured of his right to change beneficiaries at a later date and destroy the trust arrangement.[128] Thus it would not be wise to use this method in establishing an irrevocable trust.

B. Moment Trust Comes Into Existence

Originally there was controversy as to whether an insurance policy was a sufficient res to constitute the corpus of a trust. If the policy was not a sufficient res and it was the only trust property, the argument could be made that no trust came into existence until the death of the insured when the proceeds passed to the trustee, thus making the trust testamentary. Today the above argument has been refuted and virtually destroyed. Cases, with the approval of the textwriters, have held that an insurance trust is not testamentary even where the insured designates the trustee as beneficiary and retains the right to change the beneficiary or alter and revoke the trust.[129] Professor Scott in his work on trusts argues very convincingly, "It would seem that the fact that the policy is payable to a beneficiary as trustee for others makes it no more testamentary than if it were payable to the beneficiary absolutely."[130] Several states have adopted statutes expressly allowing a life insurance policy to be corpus of a trust.[131]

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[127]See Mahoney v. Crocker, 58 Cal. App. 2d 196, 136 P.2d 810 (1943).

[128]See 1A BOGERT, *op. cit. supra* note 118, § 142(a); SHATTUCK, *op. cit supra* note 108, § 7.

[129]State *ex. rel.* Citizen's Nat'l Bank v. Superior Court, 236 Ind. 135, 138 N.E.2d 900 (1956); Gordon v. Portland Trust Bank, 201 Ore. 648, 271 P.2d 653 (1954), 53 A.L.R.2d 1106 (1957); see NOSSAMAN, *op. cit. supra* note 95, § 14.01; RESTATEMENT (SECOND), TRUSTS § 57, comment f (1959); Schenck, *supra* note 104; Schwartz, *supra* note 87.

[130]SCOTT, TRUSTS § 57.3 (2d ed. 1956).

[131]*E.g.*, WIS. STAT. ANN. § 206.52(1) (1957) which provides, "It shall not be necessary to the validity of any such trust agreement or declaration of trust that it have a trust corpus other than the right of the trustee to receive such insurance proceeds as beneficiary."

Although this question has not been adjudicated in Mississippi, it is submitted that there would be no difficulty in establishing the life insurance policy as a sufficient res. The Mississippi Supreme Court has said that the interest of a beneficiary of a life insurance policy is a vested interest by common law from the issuance of the policy, and that even if common law did not apply, the insurance exemption statute saying that proceeds ". . . shall inure to the party or parties named as beneficiaries thereof. . . ." gives a vested interest.[132] Thus the vested interest of the trustee, although subject to complete divestment, should be a sufficient res.

As a word of caution, the estate planner must make certain that the insurance trust in no way depends upon the will for its efficacy as illustrated by a recent case. A husband created an inter vivos trust with insurance policies and made the amounts going to the beneficiaries dependent upon whether or not his wife renounced the will. The court, with three judges vigorously dissenting, held this arrangement to be testamentary because the trust was inoperative without the will.[133] However, so long as the trust agreement does not depend upon the will, the insurance trust arises the moment the policy is made payable or assigned to the trustee as beneficiary.

C. The Trustee, His Selection and Powers

1. *Selection of the Trustee*

The choice of a proper trustee for an insurance trust is often difficult. To aid in the proper selection, a few advantages and disadvantages of some commonly used trustees will be outlined. One must realize that different situations call for different types of trustees.

Some insurers offer policy holders their services as trustees. The insurer type trust may suit some estate plans, but this arrangement is not very flexible. It is difficult for an insurer as trustee to put the interest of the beneficiary first and at the same time guard its own interests as insurer. One can imagine the embarrassing conflict of interests resulting from a situation where there is doubt of the insurer's liability and the trustee must sue itself in order to collect proceeds. Consequently, use of the insurer as trustee can offer some real legal problems.

The insured can serve as trustee himself, but there are obvious disadvantages to this arrangement. The insured acting as trustee may find himself taxed on trust income and suffer from inclusion of the trust in

[132]Jackson Bank v. Williams, 77 Miss. 398, 26 So. 965 (1899). Statute quoted is present Miss. Code Ann. § 308 (1956); see Johnson v. Bacon, 92 Miss. 156, 45 So. 858 (1907).

[133]Bickers v. Shenandoah Valley Nat'l Bank, 197 Va. 145, 88 S.E.2d 889 (1955), *rehearing denied*, 197 Va. 732, 90 S.E.2d 865 (1956), 54 Mich. L. Rev. 880, 42 Va. L. Rev. 256.

his gross estate at death. Since the important functions of the trustee of an insurance trust arise on death of the insured, it is better that the trustee who will do the actual work be appointed rather than the insured.[134] The insured should not act as co-trustee either, as some incidents of ownership may be attributable to him, especially if the trustees are given broad discretionary powers which would permit them to shift economic benefits.[135]

The insured's wife may act as trustee, and in small estates she may be the best trustee. However, few women have had the business experience necessary for successful administration of a trust. Generally, the insured will desire that his wife be the main beneficiary and thus her capacity as trustee would be impaired. Other important considerations are the age and health of the husband and the wife. Assuming the husband and wife are about the same age, at his death his wife would have only a limited time in which she might serve as trustee; her active duties as trustee might not commence until she was physically and mentally incapable of serving. However, in the event of the husband's early death, the wife could be an excellent trustee for the children as she would know their needs better than anyone else. Another consideration is that a spouse would be more familiar with the decedent's desires. If the spouse had duties during the insured's life, she could not be his alter ego without serious tax consequences.

The estate of the insured may also be trustee, but selection of the estate as trustee is loaded with disadvantages some of which follow: (1) Liquid insurance proceeds swell the decedent's estate upon which administration fees are figured; (2) The proceeds are subjected to the claims of creditors and to the wife's statutory share of the estate; (3) The income producing potential of the proceeds is curtailed because an executor has a narow limit of investment authority; (4) The immediate use of proceeds is delayed by slow probate; (5) The executor lacks the discretion of a trustee.[136] At times it is desirable that the estate be trustee as the insured may wish to give his executor liquidity in administering the estate by this means. Before the estate is made trustee one should double-check all circumstances.

A testamentary trustee may be designated beneficiary of an insurance policy in trust. Under this arrangement the will or another instrument would name beneficiaries of the trust. Many problems arise concerning use of a testamentary trustee. If the policy is made payable to the trustee under "my" will, no beneficiaries can be ascertained until actual probate of a will; if several wills were executed, one must assume that the probated will was the will referred to in the policy. Thus, the

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[134]Barton, *The Role of Trusts in Life Insurance Planning*, 98 TRUSTS & ESTATES 16 (1959).

[135]See State Street Trust Co. v. United States, 263 F.2d 635 (1st Cir. 1959).

[136]See Barton, *supra* note 134; Schenck, *supra* note 104.

trust would be testamentary. However, if the grantor directed that the policy be payable to the trustee of "my" will of a certain date, a present trust would be created. One can easily see the problem resulting from a revocation or modification of that will.[137]

Insurance payable to a testamentary trustee in trust is a separate subject within itself and cannot be fully discussed in this paper. Only a few courts have tested such an arrangement,[138] but several states have passed statutes making a testamentary trustee a proper beneficiary of an insurance policy.[139] Some insurance companies will accept this arrangement, but there is no guarantee of a tax saving.[140] It is not recommended that one make a policy payable in trust to a testamentary trustee as beneficiary unless there is a protective statute and the grantor is not motivated by tax avoidance.[141]

A professional trustee such as a bank may be employed. The professional is a specialist having the business experience and ability needed to administer the trust. It can assist in writing the trust agreement and in avoiding pitfalls unknown to the ordinary trustee. All the time of the professional trustee would be devoted to trust matters whereas other trustees would have many other obligations, administering the insurance trust being only a side line. When the estate is large, the choice of a professional trustee becomes even more important. Utilization of a professional trustee should always be considered.

2. *Powers of the Trustee*

Before making provision for the trustee's powers, state statutes and cases interpreting them should be examined to determine their effect upon the trust. Choice of a situs could depend upon favorability of state law. For instance, even the trustee's residence in a particular state has been held sufficient to justify taxation of the trust by that state.[142]

It is important to examine statutes on investment powers. Some states have enacted statutes specifically authorizing the trustee to invest trust funds in forms of insurance contracts.[143] Mississippi has a recent statute which requires a trustee to act prudently in investments without regard to speculation and to consider probable income and safety

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[137]See Schipper, *Designating Trustee under Will as Beneficiary of Insurance—Legal Problems*, 94 TRUSTS & ESTATES 819 (1955).

[138]*Ibid.*

[139]See Barton, *supra* note 134, for discussion of a Wisconsin statute and Cooper, *Testamentary Trust for Insurance?*, 97 TRUSTS & ESTATES 113 (1958), for discussion of a Pennsylvania statute.

[140]See Barton, *supra* note 134.

[141]See Schipper, *supra* note 137. See also Schenck, *supra* note 104, for disadvantages of testamentary trustee.

[142]See Greenough v. Tax Assessors, 331 U.S. 486 (1947).

[143]See 2 FED. EST. & GIFT TAX REP. § 7263 (1960).

unless another method of investment is prescribed.[144] Insurance is not mentioned in the statute as a recommended investment, and there are no cases at the present interpreting the statute. The statutes affecting minors and accumulations should be examined. Mississippi impliedly applies the common law rule as to accumulations.[145] It would be wise to check for existence of a "pour-over" statute.

Some states, including Mississippi, have statutes which allow banks and trust companies to employ common trust funds;[146] this type statute could make administrative cost of the insurance cheaper, thus influencing selection of situs. In Mississippi, absent the possible effect of a spendthrift clause, trust estates are subject to execution just as if the beneficiary owned the estate outright.[147] If the estate is trustee, several Mississippi statutes further limit its powers.[148] In general, all of the statutes specifically affecting wills, trusts, and fiduciaries should be examined.

Necessary powers not specifically given the trustee by statute should be provided in the trust instrument. It is very important that the trustee receive all the powers he needs to fulfill the settlor's wishes. The trustee should have the power to make proof of death of the insured and do anything essential for collecting policy proceeds, even bringing suit if necessary.[149] The trustee may be given the power to purchase securities or other property from the executor as investments and make secured and unsecured loans to the executor without any liability for loss.[150] For tax reasons, the trustee should be given absolute discretion to pay debts, administration expenses, and taxes on the estate rather than be directed to do so.[151]

Some provision should be made either relieving the trustee of the duty to pay premiums or directing him to do so out of funds provided.[152] He should be given sufficient powers to prevent the policies from lapsing. Among these would be the power to borrow against the policies to pay premiums, take paid-up insurance, use principal to pay premiums, and accept additions to the trust for specific purpose of paying premiums.[153]

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[144] MISS. CODE ANN. § 421.5 (1956).

[145] MISS. CODE ANN. § 6995.5 (Supp. 1960).

[146] *E.g.*, MISS. CODE ANN. § 5198.5 (1) (1956).

[147] MISS. CODE ANN. § 849 (1956).

[148] MISS. CODE ANN. §§ 619-20 (1956).

[149] See Clements, *What Every Lawyer Should Know About Insurance Trusts*, 43 ILL. B.J. 336 (1955).

[150] *Ibid.* SHATTUCK, *op. cit. supra* note 108, § 7; Schenck, *supra* note 104.

[151] See Treas. Reg. § 20.2042-1 (b) (1958); Wolf, *Drafting an Insurance Trust*, 98 TRUSTS & ESTATES 997 (1959).

[152] See Clements, *supra* note 149.

[153] Mannheimer, Wheeler, Friedman, *An Unexplored Form of Insurance Trust*, 34 TAXES 494 (1956).

The trust agreement should also provide that the trustee is authorized to receive property designated in any manner by the settlor, regardless of where the settlor is domiciled at his death, and that the trustee is allowed to administer this property as part of the trust.[154] This would insure that the trustee was able to accept "pour-over" assets.

Provision should also be made as to the trustee's investment powers. Broad and general investment powers should include purchase of insurance;[155] but if the settlor anticipates the trustee's use of insurance as an investment in Mississippi, it would be best to give the trustee this specific power since the applicable statute does not mention insurance. If the policies are assigned to the trustee, he should be directed to notify the insurance company immediately.[156]

V. Conclusion

This paper only sketched the many intricacies and advantages of the insurance trust. Space does not permit an analysis of when insurance should be purchased or of the type and amount to be purchased. Generally speaking, one should purchase that amount of insurance which, when added to other estate assets, will maintain his family at the standard of living to which it is accustomed. Some estate planners recommend that 10 percent of the client's income be used for this purpose,[157] but this percentage will depend upon each individual

It is impossible to categorize the situations where an insurance trust should be established. Serious consideration always should be given to use of an insurance trust if the proceeds approach $25,000 to $50,000.[158] As size of the proceeds increases, use of a trust becomes more important.

It is predicted that there will be an increase in the use of the insurance trust during ensuing years. Estates are not built overnight, and insurance is the only method of providing immediate family security while an estate is being accumulated. Since the amount of insurance needed increases with the cost of living, expert management of proceeds is becoming more essential. The insurance trust will provide this expert management and will assure that proceeds are utilized to promote family security in the best manner possible. It is hoped that this paper can serve as an introductory guide for construction of an advantageous insurance trust.

James Kearney Travis, Jr.

154See Schenck, *supra* note 104; Wolf, *supra* note 151.

155See 2 Fed. Est. & Gift Tax Rep. § 7263 (1960).

156See Clements, *supra* note 149.

157See Shattuck, *op. cit. supra* note 108, § 5.

estate.

158*Ibid.*

MISSISSIPPI'S RECENT ANNULMENT ACT

I. INTRODUCTION

Until recently, this state has had no statute dealing with annulment. The practice has been for the chancery court to entertain suits for annulment "where the alleged impediment was within its inherent equity powers and where it had not been removed therefrom to become a cause for divorce by statute."[1] In a justifiable search for certainty and consistency in this area of the law, an act was recently passed to establish grounds and statutory procedure for the adjudication and annulment of marriages.[2] Certainly, the intentions behind this legislation were meritorious; however, it is submitted that the end results will not satisfy such intentions. As is often the case, a single act or piece of legislation standing alone reads well and seems to state the law categorically and unambiguously. This is also true with the act discussed herein; standing alone it appears to state the law on annulment simply and clearly. However, when read in conjunction with our divorce statutes and judicial interpretations thereof, many conflicts and inconsistencies are apparent. The purpose of this comment will be to note some of the major conflicts and inconsistencies presented in an effort to portray the need for a complete and conjunctive revamping of our laws on divorce and annulment.

II. BACKGROUND

Historically, an annulment was proper where the cause therefor existed at the time of the marriage. In other words, annulments were granted where no valid marriage ever existed or, if it did exist, it was voidable as a matter of law.[3] On the other hand, a divorce was generally considered proper where the cause therefor arose after a valid marriage.[4] To a certain extent this historical concept has been followed in our jurisdiction. For example, as a general proposition a marriage which is void or voidable for some cause existing at the time of the marriage may be set aside by a proceeding in chancery for annulment. However, this rule has been modified to a large extent by our present divorce statute.[5] Thus, a marriage which is void or voidable for some cause existing at the time of the marriage may be set aside by a proceeding in chancery for an annulment, *provided however,* that the cause therefor has not been made a statutory ground for divorce.[6] In this light, it

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[1] BUNKLEY & MORSE, AMIS ON DIVORCE AND SEPARATION IN MISSISSIPPI § 2.02 (1957) [hereinafter cited as BUNKLEY].

[2] Miss. H.B. 61 (1962).

[3] See BUNKLEY § 2.00.

[4] See *id.* § 2.02.

[5] MISS. CODE ANN. § 2735 (1956).

[6] For such causes that have been made statutory grounds for divorce see MISS. CODE ANN. §§ 2735(1), (8)-(11) (1956); BUNKLEY § 3.03.

is important to note that of the twelve causes for which a divorce may be granted, five are for causes existing at the time of the marriage.[7] Therefore prior to the passage of the present annulment act, these five causes which were common law and canon grounds for annulment were exclusively statutory grounds for divorce.[8]

III. The Annulment Act

A. Option of Annulment or Divorce

In many instances, there have been changes made by the recent act and now certain causes which are statutory grounds for divorce[9] are also within the annulment act as grounds for annulment.[10] For example, the recent annulment act provides for the annulment of bigamous and/or incestuous marriages.[11] Prior to its passage the only remedy in the case of a bigamous or incestuous marriage was by a divorce from the bonds of matrimony.[12] Thus, there now exists an option of remedies in the case of such marriages. The same is true of the ground or cause wherein the wife is pregnant by a person other than her husband at the time of the marriage and the husband did not know of such pregnancy.[13] Suffice it to say that the same situation may also exist where the cause is insanity[14] or impotency[15] of one of the parties. These causes will be discussed in detail hereafter.

It is obvious that in many instances, the same cause or ground may afford the complaining party an option of proceeding under the divorce statute or under the annulment act. Certainly, having an election of remedies is not strange to the law. However, viewed in an historical light and striving for simplicity, it is submitted that the better and more accepted procedure would be to establish certain causes as exclusive grounds for divorce and other causes whereby the sole remedy is annulment. It is further submitted that the most logical distinction would be to limit divorce to decrees wherein the causes therefor arose after a valid marriage and entertain annulment suits where the cause therefor existed at the time of the marriage.

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[7]These five causes as contained in Miss. Code Ann. § 2735 (1956), are natural impotency, insanity, marriage to another at the time of the pretended marriage between the parties, pregnancy of wife by another at the time of marriage, and relation to each other within the degrees of kindred between whom marriage is prohibited by law.

[8]See Bunkley § 3.03.

[9]Miss. Code Ann. §§ 2375 (1), (8) - (11) (1956).

[10]Miss. H.B. 61, §§ 1, 2 (a) - (c) (1962).

[11]Miss. H.B. 61, § 1 (1962).

[12]See Miss. Code Ann. §§ 2735 (9), (11) (1956).

[13]*Compare* Miss. H.B. 61, § 2 (e) (1962), *with* Miss. Code Ann. § 2735 (10) (1956).

[14]*Compare* Miss. H.B. 61, § 2 (b) (1962), *with* Miss. Code Ann. § 2735 (8) (1956).

[15]*Compare* Miss. H.B. 61, § 2 (a) (1962), *with* Miss. Code Ann. § 2735 (1) (1956).

B. Impotency

Since the passage of the recent annulment act an interesting situation has arisen in the case where dissolution of the marriage is sought on the grounds of impotency. This act establishes *incurable* impotency as a ground for annulment.[16] Prior to its passage, the only comparable ground existed in our divorce statute, wherein the injured party had a ground for divorce for *natural* impotency existing at the time of the marriage.[17] Thus, there now exists a ground for annulment where the cause is *incurable* impotency and also a statutory ground for divorce for the injured party where the cause is *natural* impotency. Historically, natural impotency was a ground for annulment by the non-impotent party.[18] Prior to the annulment act the chancery court could not grant an annulment to the impotent party because there was no statute conferring jurisdiction on that court.[19] However, some state statutes allow the impotent party to sue for an annulment when he or she did not know of the impotency at the time of the marriage.[20] Natural impotency as a ground for divorce is available only to the non-impotent party.[21] Query: Is incurable impotency a ground for annulment for the impotent or non-impotent party? Also the question arises as to the nature of *incurable* impotency. For example, is incurable impotency the same as natural impotency or does it consist of elements different from those which have been peculiar to natural impotency in the past? Certainly, these and other questions must remain unanswered until there has been a judicial interpretation of this particular ground for annulment. It is submitted that impotency existing at the time of the marriage, whether it be labeled natural or incurable, should be a ground for annulment. The problem of whether or not the ground is available to the impotent or non-impotent party, or both, could have been cleared up in a few words. Also, the recent annulment act would have been much more effective had it established impotency as a ground whereby the sole remedy was an annulment. At the present it is clear that *natural* impotency is a ground for divorce for the non-impotent party and that a ground for annulment exists within the mysterious term, *incurable* impotency.

C. Insanity

As previously noted the recent annulment act also establishes insanity as a ground for annulment.[22] In the past, where one of the parties

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[16]Miss. H.B. 61, § 2 (a) (1962).

[17]Miss. Code Ann. § 2735 (1) (1956).

[18]See, *e.g.*, Anonymous, 89 Ala. 291, 7 So. 100 (1890).

[19]See Bunkley § 2.06.

[20]See, *e.g.*, Anonymous v. Anonymous, 126 N.Y. Supp. 149 (Sup. Ct. 1910).

[21]See Sarphie v. Sarphie, 180 Miss. 313, 177 So. 358 (1937).

[22]Miss. H.B. 61, § 2 (b) (1962).

was insane at the time of the marriage and the sane spouse did not know of the infirmity, the injured party could obtain a divorce.[23] Insanity as a ground for divorce has been interpreted as being available to the sane spouse only.[24] However, the common law remedy of annulment has always remained available to the insane spouse.[25] Thus, was it intended by the recent annulment act to establish insanity as a ground for annulment for the sane spouse as is the case in the divorce statute, or was it merely intended to codify the common law by giving the insane spouse a statutory ground for annulment? Certainly, this remains for judicial interpretation. It is submitted that this ground for annulment will be available only to the insane spouse, leaving the sane spouse with the existing remedy of divorce.

D. Failure to Comply with the Conditions Precedent to the Issuance of License

By virtue of the recent annulment act there is now a statutory ground for annulment where the parties to a marriage have not fulfilled the conditions precedent to the issuance of a marriage license.[26] However, this ground is available only where any marriage affected by such failure has not been followed by cohabitation.[27] Even where there has been a failure to comply with the statutory conditions precedent to the issuance of a marriage license, if the ceremony follows in accordance with the statutory requirements and the parties cohabit thereafter, and cohabitation is prior to a suit for annulment, the marriage is valid.[28] Undoubtedly, this ground for annulment will arise most often where the parties are under the statutory age of consent.[29] In this connection, the statute dealing with the issuance of a marriage license requires that the consent of parents or guardian be obtained where either or both parties are under the statutory age of consent unless, after the issuance of the license and the solemnization of the marriage, there is cohabitation of the parties.[30] However, there are numerous other conditions precedent to the issuance of a license which are set out by statute[31] and failure to meet them could also result in grounds for annulment.

E. Voidable Marriages

Certain provisions of the section of the annulment act discussed be-

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[23]See Miss. Code Ann. § 2735 (8) (1956).

[24]See Parkinson v. Mills, 172 Miss. 784, 159 So. 651 (1935).

[25]See, *e.g.*, *ibid.*

[26]Miss. H.B. 61, § 2 (c) (1962).

[27]*Compare* Miss. Code Ann. § 461.2 (1956), *with* Miss. H.B. 61, § 2 (c) (1962).

[28]*Ibid.*

[29]See Bunkley 42-43.

[30]Miss. Code Ann. § 461 (1956).

[31]*Ibid.*

low are nothing more than a codification of the law as it existed prior to the passage of the annulment act.[32] For example, the annulment act provides that where consent to the marriage is obtained by force or fraud the marriage shall be void from the time its nullity shall be declared by a court of competent jurisdiction.[33] Since the act provides that such a marriage is void from the time its nullity is declared, it would seem to follow that the issue to such a marriage are legitimate. This conclusion is based on the premise that since such a marriage is void only from the time its nullity is declared, obviously it is only voidable, and issue born to a voidable marriage are legitimate in this jurisdiction.[34]

Even before the annulment act, duress and fraud existed as grounds for annulment in this state.[35] In the case of duress, which is synonymous with force, the courts take the view that marriage is like any other contract, and as such there must be voluntary assent to it, or there will be no binding marriage.[36] Thus, in this state, a marriage may be annulled where duress or force deprives the party of his free will.[37] Of course, the force or duress must be operative at the time of the marriage, and if the marriage was assented to for any reason other than the force or duress the marriage is valid and may not be annulled.[38]

In the case of fraud, the courts realizing marriage is similar to other civil contracts hold that fraud in the inducement of the marriage is a cause for annulment.[39] Even though fraud in the inducement is recognized as a ground for annulment in virtually all jurisdictions, the courts are not in agreement as to the degree of fraud necessary therefor. The majority of jurisdictions hold that annulment should be granted where the fraud goes to the essentials of the marriage relation.[40] Other jurisdictions are not so rigid in their standards and hold that any fraud sufficient to set aside an ordinary contract is a sufficient degree of fraud for the annulment of a marriage.[41] In this state, many grounds that would normally be considered as resting on fraud have been made separate and specific grounds for divorce and/or annulment by statute.[42]

Since our jurisdiction is not unusually strict on divorce, as are some jurisdictions,[43] it is submitted that in order for fraud to constitute a

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[32]See Miss. H.B. 61, § 2(d) (1962), wherein consent obtained by fraud and/or force is made grounds for annulment.

[33]*Ibid.*

[34]See, *e.g.*, Bass v. Ervin, 177 Miss. 46, 17 So. 673 (1936).

[35]See *Bunkley* 44-45.

[36]See MADDEN, PERSONS AND DOMESTIC RELATIONS § 8 (1931).

[37]See, *e.g.*, Marsh v. Whittington, 88 Miss. 400, 40 So. 362 (1906).

[38] See, *e.g.*, Zeigler v. Zeigler, 174 Miss. 302, 164 So. 769 (1935).

[39]See, *e.g.*, Pretlow v. Pretlow, 177 Va. 524, 14 S.E.2d 381 (1941).

[40]See MADDEN, *op. cit. supra* note 36, § 9.

[41]See, *e.g.*, Shonfeld v. Shonfeld, 260 N.Y. 477, 184 N.E. 60 (1933).

[42]MISS. CODE ANN. §§ 2735(9), (10) (1956); Miss. H.B. 61, §§ 1, 2(e) (1962).

[43]New York, for example, where the only ground for divorce is adultery.

ground for annulment the fraud must go to the essentials of the marriage relation.[44] In other jurisdictions, it has been held that the fraud therein went to the essentials of the marriage relation where one party to a marriage entered the relation with an intent not to have sexual relations with the other and this fact was unknown to the other.[45] Fraud touching the essentials of the marriage relation has also been found where one party conceals an infection with a venereal disease[46] and where there was a concealment of sterility.[47] However, fraudulent concealment or misrepresentation as to one's character, wealth, social position, previous history, or habits is not generally held to go to the essentials of the marriage relation.[48]

Since fraud and duress have existed as grounds for annulment prior to the annulment act, it is submitted that the same rules and principles applied before the act will govern in the future when the now statutory grounds of fraud and/or duress are before the courts.

Other provisions of this section[49] are not so clear as the provision declaring fraud and/or duress as grounds for annulment. In fact, a study of the subdivisions discussed below has prompted this writer to term them the most confusing and incoherent provisions of the entire annulment act. The grounds for annulment provided therein are available only in the absence of ratification and only if suit for annulment is brought within six months after the ground therefor has been or should have been discovered. It is submitted that one notable provision contained therein changes the marriage of a child under seven years of age from a void marriage to a voidable marriage. This conclusion is based on the language of this section which provides that when either of the parties to a marriage shall be incapable, from want of age or understanding, of consenting to a marriage, the marriage shall be void from the time its nullity shall be declared by a court of competent jurisdiction.[50] Thus, a child under seven years of age may enter into a marriage and such marriage will not be absolutely void as in the past,[51] but shall be void only from the time its nullity shall be declared by a court of competent jurisdiction. Of course, this feature is primarily academic, but it does seem to be an excellent illustration of the confusion and perplexities within the language of this section.

Moving now to a more realistic problem presented within this

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[44]There are no reported cases in Mississippi on fraud; however, see White v. Williams, 154 Miss. 897, 124 So. 64 (1930) (dictum); Parkinson v. Mills, 172 Miss. 784, 159 So. 651 (1935) (dictum).

[45]See, *e.g.*, Hyslop v. Hyslop, 241 Ala. 223, 2 So. 2d 443 (1941).

[46]See, *e.g.*, Turner v. Avery, 92 N.J. Eq. 473, 113 Atl. 710 (Ch. 1921).

[47]See, *e.g.*, Aufort v. Aufort, 9 Cal. App. 2d 310, 49 P.2d 620 (Dist. Ct. App. 1935).

[48]See MADDEN, *op. cit. supra* note 36, at 14-15.

[49]Miss. H.B. 61, § 2 (d) (1962).

[50]See *ibid.*

[51]See BUNKLEY 42-43.

section, a portion of the subdivision declares that "when either of the parties to a marriage shall be incapable, from physical causes of entering into a marriage, the marriage shall be void from the time its nullity shall be declared by a court of competent jurisdiction." The confusing and perplexing problem presented by this provision is in determining what causes were intended to be included thereunder. For example, the impediment existing in a miscegenetic or incestuous marriage is certainly physical in nature and therefore the parties reasonably could be considered "incapable from physical causes." Thus by the express language of this subdivision the marriage would not be absolutely void but void only from the time its nullity is declared by a court of competent jurisdiction. Also, by virtue of the dictates of this section, marriages wherein the parties are "incapable from physical causes" can only be declared a nullity in the absence of ratification and only if suit is brought within six months after the cause therefor is discovered. However, no one would argue that a miscegenetic or incestuous marriage could be ratified or that failure to bring suit within six months after the impediment was discovered would preclude the bringing of such suit. Obviously incestuous or miscegenetic marriages were not intended to be included in this part of the act because, as previously mentioned, such marriages were declared void in the beginning of this act.[52] The purpose of presenting such an extreme construction of this particular section as well as others is to portray the ambiguousness of its language and resulting confusion which lends itself to speculation and uncertainty which eventually the undeserving clients and litigants must bear.

F. Legitimation of Issue

The most surprising and certaintly the most controversial provision of the recent annulment act is that portion dealing with legitimation of issue.[53] The section provides that, with the exception of incestuous or miscegenetic marriages, the issue of the parties to a *void* marriage conceived subsequent to the date thereof are legitimate. It further provides that such issue are legitimate whether the marriage be declared void because of a prior existing marriage, or is annulled for some other cause. Attention is called to the fact that this section expressly declares that issue of the parties to a *void* marriage are legitimate. In this state, children born to a voidable marriage are considered as born during lawful marriage and therefore enjoy the same status as legitimate children[54] and a decree of nullity in no way affects their legitimacy.[55]

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[52]See Miss. H.B. 61, § 1 (1962).

[53]See Miss. H.B. 61, § 3 (1962).

[54]See, *e.g.*, Ervin v. Bass, 172 Miss. 332, 160 So. 568 (1935).

[55]See MISS. CODE ANN. § 2744 (1956).

Prior to the recent annulment act, the rule at common law,[56] and in this state,[57] was that every child not born during lawful wedlock, was illegitimate. However, the annulment act expressly declares that children to a *void* marriage also enjoy the status of legitimacy. In addition to declaring generally that children to a *void* marriage are legitimate, the annulment act goes further and specifically provides that the issue of a void marriage are legitimate, *whether the marriage be declared void because of a prior existing marriage,* or is annulled for some other cause. Obviously, this provision has the effect of legitimizing children born to a bigamous marriage. It is important to notice that by declaring such issue legitimate, this provision is in direct conflict with a section of our divorce statute which expressly provides that such issue shall be illegitimate and subject to the disabilities of illegitimate children.[58] Thus, that section of the divorce statute is necessarily repealed by virtue of the general provision of the annulment act repealing all laws in conflict therewith.[59]

The intentions behind this section of the annulment act dealing with legitimation of issue are not questioned. It is obvious that the sole purpose of this section was to further protect the status of unfortunate children born to reckless unions. However, it is submitted that in their attempt to protect such children the framers have failed to consider the overall effect of the recent legislation on other fields of the law.[60]

G. Custody of Children

Even prior to the recent annulment act, custody, support and maintenance of children, has been handled by the chancery court when dealing with annulment suits.[61] However, since the passage of the annulment act there is now statutory authority for the chancery court, in its discretion, to make all orders touching the care, custody and maintenance of the children of the marriage.[62] The act also allows the court on petition to later change the decree and make from time to time such new decree as the case may require.[63] Since the chancery court had been exercising this authority prior to the annulment act, the procedure and practice exercised heretofore is of significance. Thus, in the past, where

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[56]See, *e.g.*, Wilson v. Babb, 18 S.C. 59 (1882); Warren v. State, 26 Ala. App. 284, 158 So. 770 (1935); *In re* Paterson's Estate, 34 Cal App. 2d 305, 93 P.2d 825 (Dist. Ct. App. 1939).

[57]See BUNKLEY § 2.05 (3).

[58]MISS. CODE ANN. § 2744 (1956).

[59]Miss. H.B. 61, § 7 (1962).

[60]For instance where the question of legitimacy arises in cases concerning descent and distribution or workmen's compensation.

[61]See, *e.g.*, Ervin v. Bass, 172 Miss. 332, 160 So. 568 (1935).

[62]Miss. H.B. 61, § 4 (1962).

[63]*Ibid.*

a voidable marriage was annulled, the children were legitimate and the father was held to be primarily liable for the support of the children and the mother secondarily liable.[64] In any case where a marriage was determined to be wholly void and a decree of nullity was granted, the woman was held to be entitled to custody.[65] Also, where a decree of nullity was rendered at the woman's instance she would have the burden of the children's support.[66] However, where the husband happened to be the complainant in such a suit, it would seem that equity would require that he aid in the support of the children.[67] It is submitted that the annulment act will have no significant change as to the custody, support and maintenance of the children to an annulment suit. However, in light of the confusion brought on by the annulment act concerning void and voidable marriages and legitimation of issue, it does seem that the chancellors might have a problem in applying established principles to questions of custody, burden of support, maintenance and the like.

H. Procedure

Prior to the passage of the act, the rules of pleading and practice in annulment suits were the same as in other suits in chancery.[68] However, because of the public interest involved in every marriage, the decree of annulment had to be based on proof submitted to the court.[69] The proof could not be based on consent or on a decree pro confesso where no defense was made.[70] Since the passage of the annulment act, the same rules of pleading and procedure will apply as in divorce cases.[71] The annulment act further provides that all suits for annulment shall be tried in term time or vacation and the laws of process now in force in divorce cases in this state shall apply in all suits for annulment.[72]

Before the annulment act, the common law rule, and the rule in this state, was that "in an annulment suit, the court must have jurisdiction of the marital status, and the jurisdiction of this status was the domicile of either one or both of the parties."[73] The annulment act provides generally that the chancery court of this state shall have jurisdiction to hear and determine all suits for annulment.[74] The annulment

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[64]See, *e.g.*, Bass v. Ervin, 177 Miss. 46, 170 So. 673 (1936).
[65]See BUNKLEY 39.
[66]See *ibid.*
[67]See *ibid.*
[68]See BUNKLEY § 2.04.
[69]See, *e.g.*, Main v. Main, 113 Miss. 165, 74 So. 138 (1917).
[70]See BUNKLEY 34.
[71]See Miss. H.B. 61, § 6 (1962).
[72]See *ibid.*
[73]BUNKLEY 33.
[74]Miss. H.B. 61, § 6 (1962).

act does specifically provide for the filing of the bill for annulment.[75] It declares that "the bill for annulment shall be filed in the county where the defendant resides, or *in the county where the marriage license was issued,* or in the county where the complainant resides, if the defendant be a nonresident of this state."[76] It is submitted that in the situation where both parties are nonresidents but have married in this state no jurisdictional problem exists in the light of our jurisdictional decisions.[77]

IV. Conclusion

This is by no means, nor was it intended to be, an exhaustive examination of the recent act on annulment and its effect on the law as it existed prior to enactment. The sole purpose of this comment has been to note a few of the most obviously confusing provisions and to leave it to consideration by others as to the ultimate results and ramifications. Much of the annulment act is excellent and does much in the way of informing counsel of their clients' rights and remedies. It does, however, demonstrate the desperate need for an exhaustive study and revamping of our divorce and annulment laws in a coordinated rather than a piecemeal fashion.

Harry L. Case, Jr.

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[75]See Miss. H.B. 61, § 5 (1962).

[76]*Ibid.*

[77]See, *e.g.*, Antoine v. Antoine, 132 Miss. 442, 96 So. 305 (1923), where the court stated: "We have no statute in this state relating to the residence or domicile of the parties with reference to annulment suits. Our statutes upon divorce do not govern. In suits of this character, under the common law, the court must not only have jurisdiction of the parties, but must also have jurisdiction of the marriage status, and the jurisdiction of the domicile of either one or both of the parties."

RECENT DECISIONS

Appeal and Error—Bill of Exceptions, Time of Filing

Proceeding before the Benton County Board of Education on petition of certain children, residents of Benton County, desiring to be transferred to a school district in Marshall County. After denial of petition, petitioners appealed to the State Educational Finance Commission as permitted by statute.[1] Commission met on June 2, 1961, and sustained the petitions, but no record of the testimony was made, no written order was entered, and Commission adjourned without the minutes having been signed. Commission then met in regular session on June 19, 1961, at which meeting the minutes of June 2, 1961, were signed. On June 20, 1961, the Board of Education tendered a bill of exceptions to the Commission which was signed as amended on July 17, 1961. An appeal was taken from the order of the Commission to the Chancery Court of Benton County where appellees, the children and parents, moved to strike the bill of exceptions on the ground that it was not presented within the statutory time of ". . . during the term or within ten days . . . after the end of the term. . . ."[2] The motion was overruled and the order of the Commission sustaining the petition was affirmed. Held: Affirmed. The bill of exception was presented promptly after the minutes of the Commission were signed, well within the statutory time limitation. *Benton County Board of Education v. State Educational Finance Commission,* 138 So. 2d 912 (Miss. 1962).

Prior to 1285 only errors which appeared on the face of the record could be assigned for appellate review, even though there might be erroneous and material errors not appearing on the face of the record.[3] The bill of exceptions created by the Statute of Westminster II[4] was designed to remedy this situation.[5] It has been held that this statute is a part of the common law in the United States,[6] and it has been the model for all similar legislation in this country.[7] Statutes providing for bills of exceptions were held to be remedial in nature[8] and were liberally construed in favor of the bill in regard to its form.[9] At a later date the rule of liberal construction was extended to encompass the strict requirements concerning time.[10]

Mississippi has purported to follow a rule of strict construction of the statute providing for the bill of exceptions, both as to time and as to place and manner.[11] In construing the statute[12] the court has said that ". . . the last day of the term and the last day of the actual holding of

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[1] Miss. Code Ann. § 6246-12 (1952).

[2] Miss. Code Ann. § 1533 (1956) (which is incorporated into and made applicable to Chancery Court by Miss. Code Ann. § 1313 (1956).

[3] 1 Holdsworth, A History of English Law 223-34 (3d ed. rewritten 1922).

[4] 13 Edw. 1, ch. 31 (1285).

[5] 1 Holdsworth, *op. cit. supra* note 3, at 223-24.

[6] *E.g.,* Spurlock v. J. T. Knight & Son, 246 Ala. 33, 18 So. 2d 685 (1944).

[7] *Ibid.*

[8] *E.g.,* State *ex rel.* Winsor v. Taylor, 134 Mo. App. 430, 114 S.W. 1029 (1908).

[9] See *Ibid. Contra,* Naro v. State, 212 Ala. 5, 101 So. 666 (1924).

[10] See Beebe v. State *ex. rel.* Starr Piano Co., 106 Ohio St. 75, 139 N.E. 156 (1922).

[11] See Richmond v. Enochs, 109 Miss. 14, 67 So. 649 (1915).

[12] Miss. Code Ann. § 1533 (1956).

the court are used by the statute to mean the same thing. The end of the term is the time of final adjournment, and the date of that is conclusively fixed by the minutes of the court."[13] The State Educational Finance Commission is required to keep minutes of its proceedings[14] as are the courts of the state.[15] However, the time by which the minutes of the Commission must be signed is not provided by statute.[16] In cases construing statutes requiring that minutes be kept, the court has held that business done at a meeting at which the minutes were not signed will be given effect from the date of a subsequent meeting at which the minutes were in fact signed, provided there was actual authority to transact such business at the subsequent meeting.[17] Thus, in the noted case, the date on which the minutes were signed was the end of the term.[18] The fact that the bill was not signed promptly is immaterial since the appellant had tendered the bill as required by law.[19]

Although Mississippi apparently pays lip-service to a rule of strict construction of statutes governing the bill of exceptions, this rule has been applied slavishly only in cases where any other result would work an injustice, e.g. tax sales.[20] The result reached in the instant case is not startling in the light of the previous cases in which an analogous point was raised.

Richard Baxter Wilson, Jr.

Constitutional Law—Due Process—Right to Counsel

Petitioner, an illiterate man, was convicted in a Florida state court of the noncapital offenses of incestuous sexual intercourse with his thirteen-year-old daughter and, in a separate count relating to the same acts, with fondling a minor child. He obtained a provisional writ of habeas corpus from the Florida Supreme Court on his petition asserting that he was not afforded the assistance of counsel at the trial. Florida law does not require the court to appoint counsel to represent indigent defendants except in capital cases,[1] so the Florida Supreme Court discharged the writ.[2] Held: Reversed. The due process clause of the fourteenth amendment guarantees the assistance of counsel in a state criminal case where the lack of such assistance makes the trial unfair unless the right to counsel is intelligently and competently waived. *Carnley v. Cochran,* 82 Sup. Ct. 884 (1962).

The right to counsel in the federal courts is guaranteed in all crimi-

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[13]Jones v. Williams, 62 Miss. 183, 184 (1884).

[14]Miss. Code Ann. § 6246-10 (1952).

[15]Miss. Code Ann. § 1665 (1956).

[16]*Compare* Miss. Code Ann. § 6246-10 (1952), *with* Miss. Code Ann. § 1665 (1956).

[17]Gardner v. Price, 197 Miss. 831, 21 So. 2d 1 (1945). See also Wilson v. Eckles, 232 Miss. 577, 99 So. 2d 846 (1958); Merchants & Mfrs. Bank v. State, 200 Miss. 291, 25 So. 2d 585 (1946).

[18]*Cf.* Jones v. Williams, 62 Miss. 183 (1884).

[19]See May v. Layton, 213 Miss. 129, 55 So. 2d 460 (1951); McGee v. Beall, 63 Miss. 455 (1886).

[20]See Wilson v. Eckles, 232 Miss. 577, 99 So. 2d 846 (1958); Gardner v. Price, 197 Miss. 831, 21 So. 2d 1 (1945).

[1]Fla. Stat. Ann. § 909.21 (1944).

[2]Carnley v. Cochran, 123 So. 2d 249 (Fla. 1960).

nal prosecutions by the explicit language of the sixth amendment.[3] In 1938, the Supreme Court of the United States held that a person charged with crime in a federal court is "entitled" to the assistance of counsel,[4] and this result has been embodied in the Federal Rules of Criminal Procedure.[5] The fourteenth amendment does not incorporate the specific guarantees of the sixth amendment in state criminal proceedings,[6] but it does impose on state actions the constitutional restriction that they " . . . shall be consistent with the fundamental principles of liberty and justice which lie at the base of all our civil and political institutions."[7] In 1932, the United States Supreme Court held that the due process clause of the fourteenth amendment guarantees the right of assistance of counsel to a person charged with a capital offense in a state court.[8] Later, in *Betts v. Brady,* a non-capital case, a divided court denied the demand that in every criminal case, whatever the circumstances, a state must furnish counsel.[9] What constitutes a denial of fundamental fairness is to be tested by an appraisal of the totality of facts in each case. Later cases have modified the *Betts* rule by requiring the appointment of counsel in non-capital offenses where there exist special circumstances by which the lack of counsel results in injustice.[10]

The instant case falls within the "special circumstances" test under which the accused has a right to the assistance of counsel, if such right was not intelligently and understandingly waived by him. The court stated that the assistance of counsel might well have materially aided the petitioner in coping with several aspects of the case.[11] For instance, a lawyer, but not a layman, might have perceived that because the Child Molester Act[12] was invoked against the petitioner, a decision of the Florida Supreme Court[13] raised doubts as to the validity of the prosecution under the Florida Constitution. In addition, the Child Molester Act had included no reference to incest prior to an amendment enacted subsequent to the time of the alleged offense.[14] The Florida Court imputed to petitioner waiver of benefit of counsel, but the Supreme Court refused to accept this, holding that where the assistance of counsel is a constitutional right, such right is not lost by the lack of an affirmative

[3]See generally Holtzoff, *The Right of Counsel under the Sixth Amendment,* 20 N.Y.U.L. REV. 1 (1944).

[4]Johnson v. Zerbst, 304 U.S. 458 (1938).

[5]FED. R. CRIM. P. 44.

[6]*E.g.,* Palko v. Connecticut, 302 U.S. 319 (1937).

[7]Hebert v. Louisiana, 272 U.S. 312, 316 (1926).

[8]Powell v. Alabama, 287 U.S. 45 (1932).

[9]Betts v. Brady, 316 U.S. 455 (1942); *accord,* Foster v. Illinois, 332 U.S. 134 (1947). *Contra,* 47 MICH. L. REV. 705 (1949); 10 U. PITT. L. REV. 232 (1948); 26 TEMPLE L.Q. 86 (1952).

[10]Smith v O'Grady, 312 U.S. 329 (1941) (plea of guilty because of state officers' deception); House v. Mayo, 324 U.S. 42 (1945) (no reasonable opportunity to consult with attorney); Uveyes v. Pennsylvania, 335 U.S. 437 (1948) (inexperienced youth); Wade v. Mayo, 334 U.S. 672 (1948) (unfamiliarity with court procedure); Townsend v. Burke, 334 U.S. 736 (1948) (prosecution's submission of misinformation); Gibbs v. Burke, 337 U.S. 733 (1949) (trial mistakes in procedure).

[11]Carnley v. Cochran, 82 Sup. Ct. 884, 885 (1962).

[12]FLA. STAT. ANN. ch. 801, §§ 801.01-.16 (Supp. 1961).

[13]Copeland v. State, 76 So. 2d 137 (Fla. 1954).

[14]Fla. Laws Ex. Sess. 1957, ch. 57-1990, § 1.

request. Mr. Justice Black, in a concurring opinion,[15] said that he would overrule the "shocking to the universal sense of justice" standard of *Betts v. Brady*. He would recognize that defendants in state courts have by reason of the fourteenth amendment the same unequivocal right to counsel as defendants in federal courts have by virtue of the sixth amendment. Mr. Justice Douglas, concurring,[16] emphasized that intricate procedural rules in a criminal trial face a layman with a labyrinth he can never understand. "As a result, the jury system—pride of the English-speaking world—becomes a trap for the layman because he is utterly without ability to make it serve the ends of justice."[17]

The noted case does not overrule *Betts v. Brady*. Twenty years application of the *Betts* rule has shown, in the words of Mr. Justice Black, "its basic failure as a constitutional guide."[18] As time has passed, the Supreme Court has been compelled under the *Betts* rule to reverse more and more state convictions. This case forms part of the growing recognition that no layman should be compelled to defend himself in a criminal prosecution. The basis for the desire to overrule *Betts* and assure legal counsel in all criminal cases has often been predicated on the premise that the due process clause of the fourteenth amendment incorporates all the first eight amendments, including the sixth amendment. This has erected a hurdle in the minds of those who are reluctant to go that far. Perhaps the same result may be achieved by the recognition that need of counsel in all criminal cases is a necessary component to a fair trial, not linked necessarily to the sixth amendment, but rather that it is a requisite to ordered liberty.

Sylvester John Hemleben

Constitutional Law—Justiciability of Legislative Reapportionment Under the Fourteenth Amendment

Qualified voters of certain counties of Tennessee brought an action in the Federal District Court, alleging that apportionment of the state legislature denied plaintiffs and others in a similar situation equal protection of the laws under the fourteenth amendment to the federal constitution. The complaint was dismissed on the grounds that the court lacked jurisdiction of the subject matter, that complainants failed to state a claim upon which relief could be granted, and that indispensable parties defendant were not present in court. Held: Reversed. The lower court possessed jurisdiction of the subject matter and plaintiffs presented a justiciable case and had standing to sue. *Baker v. Carr,* 82 Sup. Ct. 691 (1962).

One duty of a court confronted with an alleged political question is to determine whether the constitution has confided the subject to a nonjudicial branch of the government and if so, whether that branch has exceeded its authority.[1] One must analyze cases from all governmental areas to identify the "analytical threads"[2] that create the doctrine

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[15]Carnley v. Cochran, 82 Sup. Ct. 884, 892 (1962).

[16]*Ibid.*

[17]*Id.* at 894.

[18]*Id.* at 891.

[1]*Cf.* Coleman v. Miller, 307 U.S. 433 (1939).

[2]Baker v. Carr, 82 Sup. Ct. 691 (1962).

of the political question. For example, authority over foreign relations is a power delegated to the President.[3] Broad statements have been made that all issues concerning foreign relations are political,[4] but there are exceptions.[5] Many issues concerning validity of enactments and the enactment process have been refused because they created a political issue,[6] but the court has not hesitated to seek an effective date in the legislative journals if one did not appear on the statute.[7] The court has consistently refused to consider matters of structure and organization of the political institution of a state.[8] Since the famous Rhode Island Case[9] the court has refused to resort to the guaranty clause in actions against state[10] or federal[11] officers because of the nonjusticiability rule. Jurisdiction over abstract questions of political power, of sovereignty and of government has been refused by the court.[12] The court has declined to use equity powers to enjoin a state in the dismissal of a public officer.[13] The judicial standards of the fourteenth amendment have been open to the court since 1868, but the question has been whether under the facts the state's action was reasonable.[14]

There has been a long series of cases invoking the equal protection clause of the fourteenth amendment to restrict the power of the states to fix the electoral weight of their various subdivisions.[15] The leading case prior to the present decision held that such a complaint was nonjusticiable because first, the federal judiciary could not become involved in matter traditionally left to the state legislature; second, it was difficult to apply a judicial standard to the problem; third, it was difficult to offer an adequate remedy.[16] Since that time the court has consistently held that such claims amounted to a political issue.[17] The court has dismissed an appeal challenging under the equal protection clause an Illinois legislative reapportionment.[18] An attack on municipal voter districts of unequal size,[19] as well as one upon the Georgia county unit plan,[20] was dismissed for want of a substantial federal question. "Federal courts consistently refuse to exercise their equity powers in cases posing political issues arising from a state's geographical distribution of electoral strength among its political subdivisions."[21] Only five years ago the

[3] U. S. CONST. art. II, § 2.

[4] *E.g.*, Oetjen v. Central Leather Co., 246 U.S. 297 (1918).

[5] See, *e.g.*, Vermilya-Brown Co. v. Connell, 335 U.S. 377 (1948).

[6] *E.g.*, Coleman v. Miller, 307 U.S. 433 (1939).

[7] See Gardner v. Collector, 6 Wall. (73 U.S.) 499 (1867).

[8] See, *e.g.*, Wilson v. North Carolina, 169 U.S. 586 (1898).

[9] Luther v. Borden, 7 How. (48 U.S.) 1 (1848).

[10] See, *e.g.*, Marshall v. Dye, 231 U.S. 250 (1913).

[11] *E.g.*, Georgia v. Stanton, 6 Wall. (73 U.S.) 50 (1867).

[12] See, *e.g.*, Massachusetts v. Mellon, 262 U.S. 447 (1923).

[13] *E.g.*, *In re* Sawyer, 124 U.S. 200 (1888).

[14] Baker v. Carr, 82 Sup. Ct. 691, 715 (1962).

[15] See, *e.g.*, Colegrove v. Green, 328 U.S. 549 (1946).

[16] *Ibid.*

[17] See, *e.g.*, Renny v. Smith, 102 F. Supp. 708 (E.D. Pa. 1951). *aff'd*, 342 U.S. 916 (1952) (per curiam).

[18] Colegrove v. Barrett, 330 U.S. 804 (1947) (per curiam).

[19] Tedesco v. Board of Supervisors, 339 U.S. 940 (1950) (per curiam).

[20] Cox v. Peters, 342 U.S. 936 (1952) (per curiam).

[21] South v. Peters, 339 U.S. 276, 277 (1950).

Supreme Court unanimously affirmed the dismissal of a complaint similar to the present one on the authority of the above cited cases.[22] The line of cases beginning with *Colegrove v. Green*[23] represents a settled rule of law the roots of which go deep into political history. In his dissenting opinion in the instant case, Mr. Justice Frankfurter concluded that "the present case involves all of the elements that have made the Guarantee Clause cases non-justiciable. It is, in effect, a Guarantee Clause claim masquerading under a different label."[24] Justice Frankfurter reviewed the history of reapportionment and concluded that legislative apportionment has always been outmoded and that undoubtedly it has always been considered a political question.[25] Detailed studies of reapportionment disclose that the trend in this century has been away from the population standard to other standards.[26] These studies also suggest that reapportionment can not be carried out equitably.[27] "Manifestly, the Equal Protection Clause supplies no clearer guide for judicial examination of apportionment methods than would the Guarantee Clause itself."[28]

There is little doubt that Justice Frankfurter was correct in stating that the former line of cases has been overruled. The reasons offered by Justice Brennan for distinguishing these cases fail to persuade. In the present case the court has broken a uniform practice by intervening in the states' political scheme. One cannot tell at this time just how far the court is going to take this new principle. From the controlling opinion it is difficult to ascertain what the test will be in future apportionment cases. The test under the equal protection clause has always been one of reasonable classification. Apparently the court must either continue the reasonableness test or create a new test for apportionment cases under the fourteenth amendment. Should it do the latter the apportionment cases would then have a standard peculiar to themselves.

Thomas Laurance Stennis II

Constitutional Law—Official Prayer in Public Schools

Plaintiffs, the parents of pupils in the public schools of New York, brought an action to compel the board of education to discontinue the use of an official prayer which acknowledged a dependence upon God and invoked His blessing upon the students, their parents, teachers, and country. Parents asserted that the prayer was contrary to the beliefs, religions or religious practices of their children and themselves and argued that the use of this officially composed prayer to open each school day constituted an establishment of religion which is prohibited by the first amendment of the United States Constitution. The Court of Appeals of New York reaffirmed the uniform position of the lower state courts in upholding the action of the school board. Held: Reversed. The promulgation of prayer by the Board of Regents and the use of

[22]Kidd v. McCanless, 352 U.S. 920 (1956) (per curiam).

[23]328 U.S. 549 (1946).

[24]Baker v. Carr, 82 Sup. Ct. 691, 754 (1962).

[25]Id. at 756.

[26]*Ibid.*

[27]*Ibid.*

[28]*Id.* at 767.

the school system to encourage the recitation of such prayer is in violation of the Constitution even though participation in the exercise is voluntary. *Engel v. Vitale,* 82 Sup. Ct. 1261 (1962).

Only in fairly recent times has the question of religious activity under the sponsorship of the several states come before the Supreme Court. While religious freedoms were held to be protected from state action in 1940,[1] six years later the *Everson* case first declared that the establishment clause of the first amendment is incorporated in the fourteenth and thereby made effective against the states.[2] The "wall of separation" which had earlier been erected between the church and the federal government[3] was not to be breached by the individual states.[4] Since that time, whenever the court has found evidence that tax-supported facilities were being used for religious instruction or that the compulsory attendance laws were forcing public school students to engage in religious activities contrary to their own beliefs, such programs have been struck down.[5]

Prior to consideration of the noted case, the court had primarily confined its hearings in this area to "released time" programs.[6] The constitutionality of requiring each day to be opened with the reading of the Bible and the recitation of the Lord's Prayer did come before the court, but was dismissed without consideration on the merits because the plaintiff's child had graduated, thus rendering the question moot.[7] In reaching the conclusion in the instant case, Mr. Justice Black observed in the majority opinion that "the constitutional prohibition against laws respecting an establishment of religion must at least mean that in this country it is no part of the business of government to compose official prayers for any group of the American people to recite as a part of a religious program carried on by government."[8] Neither the fact that a prayer may be denominationally neutral nor that participation on the part of the students is voluntary will serve to free it from these constitutional objections.[9] Both Mr. Justice Douglas in his concurring opinion,[10] and Mr. Justice Stewart in his dissent,[11] cite numerous instances of governmental support of religious activities in the Congress, the Armed Forces, the military academies, and even in the opening invocation of the Supreme Court itself. Perhaps a footnote to the majority opinion stating that those activities which are ceremonial or patriotic in nature would not fall under the prohibitions of this holding[12] was intended to be a partial answer to these references.

It seems apparent that both of the elements found to be objection-

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[1]See Cantwell v. Connecticut, 310 U.S. 296 (1940).

[2]Everson v. Board of Educ., 330 U.S. 1 (1946).

[3]See, *e.g.,* Reynolds v. United States, 98 U.S. 145, 164 (1878).

[4]Everson v. Board of Educ., 330 U.S. 1, 18 (1946).

[5]See Illinois *ex rel.* McCollum v. Board of Educ., 333 U.S. 203 (1948); 33 MISS. L.J. 251 (1962).

[6]See, *e.g.,* Zorach v. Clauson, 343 U.S. 306 (1952).

[7]Doremus v. Board of Educ., 342 U.S. 429 (1952).

[8]Engel v. Vitale, 82 Sup. Ct. 1261, 1264 (1962).

[9]*Id.* at 1266.

[10]*Id.* at 1270.

[11]*Id.* at 1274.

[12]*Id.* at 1269 n.21.

able in earlier decisions are present in the noted case, namely, the use of governmental facilities for religious instruction and a degree of compulsion, however subtle. Since each of the cases in this area has been decided on extremely narrow grounds, all that can be said with certainty is that *officially* composed prayers as a part of a religious program in the public schools is unconstitutional. It is equally apparent that this suit and others which have dealt with religious activity on the part of both state and federal governments have left many questions unanswered. While those activities referred to by Justices Douglas and Stewart may well be in support of religion, the court has not yet had occasion to rule on their constitutionality. Further, it is unlikely that the constitutionality of opening each day in Congress with prayer will ever be challenged since only members of Congress would likely have standing to sue.[13] In addition, several of these activities might be deemed to be ceremonial or patriotic rituals and outside the scope of the noted decision. There are two cases now before the Supreme Court which should decide the constitutionality of a Pennsylvania statute requiring Bible reading in the public schools[14] and a Baltimore school board regulation requiring both a Bible reading and recitation of the Lord's Prayer.[15] Both of these questions have received diverse treatment in the lower courts with many of the cases going off on the determination of whether a particular translation of the Bible is a sectarian document.[16] If the court finds that the Bible, with its many conflicting versions, is sectarian in nature, this determination, coupled with the two criteria set forth above, might be deemed sufficient to compel the court to rule these programs unconstitutional also.

Fred E. Moss

Federal Procedure—Venue—Right to Transfer Case Brought in Wrong Venue

Plaintiff brought a private anti-trust action against defendants in the Federal District Court for the Eastern District of Pennsylvania. The court could not obtain jurisdiction over several codefendants as they were not amenable to service in that district. Rather than dismiss the case, the court transferred the action to the Federal District Court for the Southern District of New York under the authority of §1406(a) of the Judicial Code. The New York court dismissed the action on the ground that the Pennsylvania court could not transfer without first having acquired jurisdiction over the defendants. The Court of Appeals for the Second Circuit affirmed. Held: Reversed. It is permissible to transfer a case brought in the wrong district or venue to one in which it could have been brought, even if the first court could not obtain jurisdiction over the defendant. *Goldlawr, Inc. v. Heiman*, 82 Sup. Ct. 913 (1962).

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[13]See Frothingham v. Mellon, 262 U.S. 447 (1923).

[14]Schempp v. School Dist., 177 F. Supp. 398 (E.D. Pa. 1959), *cert. granted*, 31 U.S.L. Week 3108 (U.S. Oct. 9, 1962) (No. 142).

[15]Murray v. Curlett, 179 A.2d 698 (Md. 1962), *cert. granted*, 31 U.S.L. Week 3108 (U.S. Oct. 9, 1962) (No. 119).

[16]*E.g.*, Gideons Int'l v. Tudor, 348 U.S. 816 (1954); see Annot. 42 A.L.R.2d 742 (1955).

Prior to the enactment of the new Judicial Code,[1] when an action was brought in the wrong venue, the court was required to dismiss the case.[2] After passage of the new Judicial Code, two statutes permitted transfer: §1404 (a), which broadened the old concept of forum non conveniens,[3] and §1406 (a), which was an entirely new concept. Section 1406 (a) required transfer for an action brought in the wrong venue but was amended in 1949 to give the court the option of transferring the case in "the interest of justice" or of dismissing it. The similarity between §§1404 (a) and 1406 (a) caused a great deal of confusion, and frequently when the courts would grant a transfer, both sections would be cited as authority.[4]

Shortly after the enactment of the Judicial Code of 1948, the transfer of a case by the lower court, sua sponte, was upheld on appeal.[5] Transfer had been ordered despite the fact that the lower court could not obtain jurisdiction over the defendant who had moved for dismissal.[6] The Court of Appeals for the District of Columbia also held it immaterial whether the transferor court could obtain jurisdiction over the defendant since transfer would promote the ends of justice.[7] The reasoning of this line of cases is that transfer rather than dismissal is preferable when the latter would terminate the rights of the plaintiff who inadvertently has chosen the wrong venue.[8] Other courts have held that there could be no transfer when jurisdiction of the person of the defendant is not obtained in a cause commenced in the wrong venue.[9] This line of cases is based on common law concepts of jurisdiction.[10]

There is no historical basis for jurisdiction in this case. On the other hand, Congress could expand the jurisdiction of the federal courts with complete disregard for state boundaries.[11] The instant case seems to solidify the criteria for a transfer under §1406 (a). It is now the law that where the plaintiff in good faith has brought his action in the wrong venue, jurisdiction over the person is not necessary for purposes of transfer. Dismissal of the case could cause the plaintiff to lose his remedy by the tolling of the statute of limitations. This decision allows the plaintiff to file his action where the venue is questionable without risking this loss of remedy. Although this seems equitable, it unfortunately permits the plaintiff to pick a venue with favorable judicial precedents while running no greater risk than having his action transferred to another district or division.

Joseph D. Gordon, Jr.

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[1] 28 U.S.C. (1948).

[2] *E.g.*, Camp v. Gress, 250 U.S. 308 (1918).

[3] See, *e.g.*, Leopard Roofing Co. v. Asphalt Roofing Indus. Bureau, 190 F. Supp. 726 (E.D. Tenn. 1960).

[4] See, *e.g.*, Internatio-Rotterdam v. Thomsen, 218 F.2d 514 (4th Cir. 1955); *cf.* Orzulak v. Federal Commerce & Nav. Co., 168 F. Supp. 15 (E.D. Pa. 1958)

[5] Schiller v. Mit-Clip Co., 180 F.2d 654 (2d Cir. 1950).

[6] *Ibid.*

[7] Amerio-Contact Plate Freezers, Inc. v. Knowles, 274 F.2d 590 (D.C. Cir. 1960).

[8] See, *e.g.*, Dennis v. Galvanek, 171 F. Supp. 115 (M.D. Pa. 1959).

[9] *E.g.*, Hohensee v. News Syndicate, Inc. 286 F.2d 527 (3d Cir. 1961).

[10] *Id.* at 530.

[11] *Cf.* 28 U.S.C. § 2361.

Income Taxation—Taxable Gain Found on Appreciated Property Given in a Divorce Settlement

In 1954 petitioner and his wife entered into a voluntary property settlement and separation agreement. In specific settlement of their property it was agreed that the petitioner would transfer to his wife 1000 shares of stock, and in consideration for this the wife promised to relinquish all claims and rights whatsoever against the husband. This agreement was incorporated into the divorce decree. In 1955, 500 shares of the stock were delivered bearing a cost basis of $74,775.37, and a fair market value of $82,250. The lower court reversed a ruling of the Commissioner that there was a taxable gain on the transfer. Held: Reversed. A transfer of appreciated property by a husband to former wife in consideration for the relinquishment of marital rights is a taxable gain and the value of the rights is ascertainable. *United States v. Davis,* 82 Sup. Ct. 1190 (1962).

Income derived from dealings in property is includible in gross income.[1] The amount of taxable income is determined by deducting the taxpayer's basis for the property from the amount realized on the sale or other disposition of the property, and the amount realized from the disposition is defined as "the sum of any money received plus the fair market value of the property (other than money) received."[2] In divorce property settlements involving the transfer of appreciated property for the relinquishment of a spouse's marital rights, the courts have generally held such rights to be property of value subject to a taxable gain.[3] Even though the gain is an intangible economic benefit, it nevertheless satisfies the statutory requirement that property be received.[4] The essential dispute permeating such cases has been the measurement of the economic gain received by the husband. In an arm's length transaction to measure the value of the economic gain the fair market value of the property given may be equated to that of the property received.[5] The Third Circuit stated that ". . . a man who spends money or gives property of a fixed value for any unliquidated claim is getting his money's worth."[6] This test, sometimes called the equal values test, was sustained in a later decision involving the transfer of stock to employees in consideration for services rendered. The court stated that there was no literal receipt of property or money but that taxable gain could be computed since the value of the services received could be measured by the value of the securities transferred.[7] Where the release of an option to purchase stock was exchanged for the relinquishment of marital rights the equal values test was applied in a decision determining that an economic gain had been realized by the holder of the option.[8] In 1960 the

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[1] Int. Rev. Code of 1954, § 61 (a) (3).

[2] Int. Rev. Code of 1954, § 1001 (a) (b).

[3] See, *e.g.*, Commissioner v. Mesta, 123 F.2d 986 (3d Cir. 1941), *cert. denied*, 316 U.S. 695 (1942); Commissioner v. Halliwell, 131 F.2d 642 (2d Cir.), *cert. denied*. 319 U.S. 741 (1942).

[4] Int. Rev. Code of 1954, § 1001 (b).

[5] Commissioner v. Mesta, 123 F.2d 986 (3d Cir. 1941), *cert. denied*, 316 U.S. 695 (1942).

[6] *Id.* at 988.

[7] International Freighting Corp. v. Commissioner, 135 F.2d 310 (2d Cir. 1943).

[8] Homer H. Marshman, 31 T.C. 269 (1958).

Sixth Circuit rejected the equal values rule. The court concluded that fair market value in such an exchange could be determined only between a willing seller and a willing buyer in the absence of compulsion and other influencing considerations.[9] The Sixth Circuit weakened its position on the equal values rule in a later decision holding that economic benefit received by a corporation transferring appreciated property to the company's pension plan should be valued by equating it to the value of the property transferred.[10] The Court of Claims added to the conflict of authority in a decision following the reasoning of the Sixth Circuit in its rejection of the equal values rule.[11]

In the instant case the Supreme Court followed the settled state of law in the lower courts in holding that the transaction was a taxable event. As to the question of greatest conflict, the measurement of the taxable gain, the Court presents several reasons for employing the equal values test. First, since the parties acted at arm's length, they must have considered the marital rights and the property transferred to be equal in value.[12] Second, an approximation of the taxable gain is more in keeping with the purpose of the tax statute than to ignore the transaction as a non-taxable event.[13] Finally, the equal values rule solves the problem of the determination of the wife's tax basis for the property received.[14] The above reasons are little more than a restatement of the reasoning of prior decisions which reached similar results.

The instant opinion does little to clarify the existing confusion in the Courts of Appeals and the Court of Claims. The contrary lines of authority are not distinguished in any significant manner, but there is simply a resounding of the reasoning of the lower courts. Either a classification of the type cases to which the equal values rule can be applied or a formalization of concrete standards governing the application of this test appears necessary. However, the fundamental holding seems to be correct. Income taxation is a practical matter. A taxable gain should not go untaxed on account of strict statutory construction.

Charles Ray Davis

Judgment Lien—Relation Back in Mississippi

After a suit was begun by a creditor, but before judgment had been rendered, the debtor conveyed certain real property to a third party for a valuable consideration. The grantee neglected to record the deed until the day after judgment had been rendered against the debtor. The judgment was subsequently enrolled by the clerk within twenty days after the adjournment of the term of court as prescribed by statute. In a suit brought by the judgment creditor to set aside the alleged fraudulent conveyance, the Chancellor decided that the judgment creditor's lien had priority over the deed of the judgment debtor's grantee. Held: Reversed. As between the judgment creditor and third parties, a judg-

[9]Commissioner v. Marshman, 279 F.2d 27 (6th Cir. 1960).

[10]United States v. General Shoe Corp., 282 F.2d 9 (6th Cir. 1960).

[11]Davis v. United States, 287 F.2d 168 (Ct. Cl. 1961), *modified,* 82 Sup. Ct. 1190 (1962).

[12]82 Sup. Ct. at 1194.

[13]*Ibid.*

[14]Id. at 1195.

ment that is properly enrolled attaches as a lien on the real property of the judgment debtor, and such lien takes effect and has priority only from the date of its enrollment. *Herrington v. Heidelberg,* 141 So. 2d 717 (Miss. 1962).

Prior to modification by statute, a judgment imposed no lien upon the real property of the judgment debtor in most states.[1] Since judgment liens exist only as a result of legislation,[2] the statutes creating them should be construed strictly.[3] The effective time of attachment of a judgment lien depends on the provision of the statute creating the lien.[4] In most jurisdictions the lien dates from the time that the judgment is docketed[5] or filed with the recording clerk.[6] Other state statutes provide that the lien created by the judgment dates from rendition thereof.[7] In a few states the lien of a judgment is held to relate back and have priority from the first day of the term during which the judgment was rendered.[8] Generally, a judgment does not attach as a lien on property which is disposed of in good faith by the judgment debtor before the rendition of a judgment.[9] However, the transferee thereof must comply with the recording statutes since the lien of a judgment creditor will attach to the interest in property that the records show to be in the judgment debtor,[10] even though the debtor has in fact transferred his interest to an innocent purchaser.[11]

The case at bar forced the court to construe § 1555 of the Code.[12] The statute states in essence that if a judgment is enrolled within twenty days of the adjournment of the term of court during which it was rendered, such judgment attaches as a lien on the property of the judgment debtor and is effective from the rendition thereof.[13] Where a judgment was not enrolled as prescribed by law,[14] it was held that the lien would not relate back and have priority from the date of rendition, but the reason for the holding was that the judgment was not enrolled within the period required.[15] It could therefore be inferred that if the judgment had been properly enrolled, the lien would have related back to the rendition and been effective against the judgment debtor's property from that date. There is only one case that can be found where the court actually gave effect to the doctrine that the priority of a judg-

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[1]See, 2 FREEMAN, LAW OF JUDGMENTS § 916 (5th ed. 1930).

[2]See, *e.g.,* Jeffrey v. Moran, 101 U.S. 285 (1879).

[3]See, *e.g.,* Mitchell v. Wood, 47 Miss. 231 (1872).

[4]2 FREEMAN, *op. cit. supra* note 1, § 918.

[5]See, *e.g.,* N.C. GEN. STAT. § 1-234 (1953).

[6]See, *e.g.,* ALA. CODE tit. 7, § 588 (1958).

[7]See, *e.g.,* ILL. ANN. STAT. ch. 77, § 1 (Smith-Hurd 1934).

[8]See, *e.g.,* Cleveland Ry. v. Williams, 115 Ohio St. 584, 155 N.E. 133 (1926).

[9]See, *e.g.,* Oliver v. Henry Quellmalz Lumber & Mfg. Co., 170 Ark. 1029, 282 S.W. 355 (1926).

[10]See, *e.g.,* Hayes v. Carey, 287 Ill. 274, 122 N.E. 524 (1919).

[11]See, *e.g.,* Miller v. Kemp, 157 Va. 178, 160 S.E. 203 (1931). *Contra, e.g.,* Mueller v. Novelty Dye Works, 273 Wis. 516, 78 N.W.2d 881 (1956).

[12]MISS. CODE ANN. (1956).

[13]MISS. CODE ANN. § 1555 (1956).

[14]MISS. CODE ANN. § 1554 (1956).

[15]See Johnson v. Cole Mfg. Co., 144 Miss. 482, 110 So. 428 (1926); *accord,* Kalmia Realty & Ins. Co. v. Hopkins, 163 Miss. 556, 141 So. 903 (1932).

ment lien relates back to the rendition of the judgment, and no indication was given that third parties should be treated any differently from the judgment debtor as regards the operative date of the lien.[16] It should also be noted that the Mississippi recording statutes[17] have been construed to apply with as much force to judgment creditors as to subsequent purchasers or encumbrancers.[18]

It is difficult to locate authority for the conclusion reached by the court in the *Herrington* case. The decision, although it may be practical, does not seem to reflect the intention of the legislature as set down in the judgment lien statute. The court says that the relation back doctrine cannot be given effect without considering the recordation statutes. Is it proper to consider the recording statutes in determining the rights of the judgment debtor's grantee, and to ignore the statutes when deciding on the position of the judgment creditor? A judgment is not a conveyance, and the recording statutes pertain only to conveyances. In attempting to reconcile the recording statutes and the judgment lien statute, the court apparently has combined them. Nevertheless, the decision brings the Mississippi law more in line with the position taken in most other states. It will also tend to alleviate the grantee's burdensome task of searching numerous records to determine whether or not it would be possible for a deed to be encumbered by the relation back of a judgment lien.

William Thad Cochran

PROPERTY—PARTITION—TESTAMENTARY RESTRICTIONS

Bill for partition brought by owner of an undivided one-half interest in real estate. Both complainant and defendant had acquired a one-fourth interest in the property from their father. Later, the mother devised her one-half interest in equal parts to complainant and defendant and provided in her will: "The above property can be sold only by mutual consent of the parties involved." Complainant charged that the land was incapable of division in kind and sought a sale. Defendant answered that the land could not be sold because of the provision in the will. The trial court sustained complainant's motion to strike all reference in the answer to such provision as being insufficient to constitute a defense. HELD: Affirmed and remanded. The mother, by her will, could not deprive complainant of the right to partition which he acquired from his father. *Holliday v. Hedge,* 139 So. 2d 866 (Miss. 1962).

It is frequently stated that every cotenant is entitled as a matter of right to partition and that this right is an absolute right "which yields to no consideration of hardship and inconvenience."[1] This statement, however, is subject to several qualifications. It is competent for cotenants to enter into agreements modifying or limiting the right to partition[2] and generally a court will not award partition in violation of a

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[16]Clark v. Duke, 59 Miss. 575 (1882).

[17]MISS. CODE ANN. §§ 867-69 (1956).

[18]See, *e.g.*, Mississippi Valley Co. v. Chicago, St. L. & N. O. R.R., 58 Miss. 846 (1881); Burkett v. People's Bank, 225 Miss. 291, 83 So. 2d 185 (1955).

[1]Smith v. Brasseale, 213 Ala. 387, 105 So. 199, 200 (1925).

[2]See, *e.g.*, Michalski v. Michalski, 50 N.J. Super. 454, 142 A.2d 645 (Super. Ct. 1958).

restriction imposed by a deed of the person through whom the person asking partition claims.[3] Testamentary provisions prohibiting or postponing partition for a reasonable time are generally upheld as not involving a direct restraint on alienation[4] since it does not restrict the transfer of the cotenant's undivided share.[5] The general rule in such cases is that effect will be given to the intention of the testator as expressed in the will.[6] However, if the provision or agreement is for the perpetual forebearance of a suit for partition, it is void as contrary to the policy of the law which maintains the right to partition as an absolute right.[7] If a restriction in a will or deed allows the transfer of a cotenant's share only if the other cotenants[8] or third parties[9] consent, this qualification is generally ignored if the restriction in itself operates as a restraint on alienation. At common law the courts had no authority to order the sale of the property and partition in kind was the only remedy.[10] Today, statutes providing for the sale of property in partition proceedings exist in every state.[11] The Mississippi statute provides that a sale can be made if it will better promote the interest of all parties than will a partition in kind, or if an equal division cannot be made.[12] The statute is construed to be an innovation on the common law,[13] and it is error to order a sale without first determining the susceptibility of the tract's being divided in kind.[14]

Partition has been denied by the Mississippi court because of testamentary restrictions when the one demanding partition had acquired his entire interest under a will containing such restrictions. For example, in *Ford v. Smith*,[15] the court held: "It is competent for a person making a will to prevent the alienation or disposition of property during the time that restrictions may be made under the . . . donee statute."[16] The *Ford* case can be distinguished in that the complainant in the noted case acquired only a part of his interest in the property through the will permitting sale "only by mutual consent". One court, in considering this problem, allowed partition, although five-sixths of cotenant's interest was acquired under a will prohibiting partition or sale.[17] The court held that in acquiring a one-sixth interest unaffected by the will, the cotenant had the right to bring an action for partition of the entire estate. Other cases have held that a tenant in common cannot, by creating a contingent remainder or entailing his estate, deprive the other cotenants of their right to partition[18] and that one

[3] *E.g.*, Hunt v. Wright, 47 N.H. 396 (1866).

[4] *E.g.*, Dee v. Dee, 212 Ill. 338, 72 N.E. 429 (1904).

[5] *E.g.*, Porter v. Tracey, 179 Iowa 1295, 162 N.W. 800 (1917).

[6] See, *e.g.*, Harris v. Harris, 138 Ore. 243, 6 P.2d 230 (1931).

[7] *E.g.*, Smith v. Brasseale, 213 Ala. 387, 105 So. 199 (1925).

[8] See, *e.g.*, Mills v. Blakelin, 307 Mass. 542, 30 N.E.2d 873 (1941).

[9] See, *e.g.*, Winn v. William, 292 Ky. 44, 165 S.W.2d 961 (1942).

[10] FREEMAN, COTENANCY AND PARTITION § 563 (2d ed. 1886).

[11] See 2 AMERICAN LAW OF PROPERTY § 6.26 (Casner ed. 1952).

[12] MISS. CODE ANN. § 965 (Supp. 1960).

[13] Cox v. Kyle, 75 Miss. 669, 23 So. 518 (1898).

[14] *E.g.*, Blake v. St. Catherine Gravel Co., 218 Miss. 713, 67 So. 2d 712 (1953).

[15] 162 Miss. 138, 146, 137 So. 482, 484 (1931).

[16] MISS. CODE ANN. § 838 (1956).

[17] Adams v. McKee, 121 Misc. 215, 200 N.Y. Supp. 765 (Sup. Ct. 1923).

[18] *E.g.*, Heiden v. Howes, 77 Ohio App. 575, 37 N.E.2d 641 (1945).

cotenant, by making a disposition of his property by deed or will containing a clause prohibiting sale, cannot take from his cotenants the right to have the property sold if indivisible.[19]

Complainant's acceptance of the one-fourth "fettered" interest should not waive his absolute right to partition since he previously had received a one-fourth interest in the property with no such restrictions. The general rule supporting testamentary prohibitions of partition appears to apply only when all rights of the parties are fixed by the provisions of the will under which title is claimed.[20] Furthermore, since actual partition is a matter of absolute right, partition by sale is a matter of absolute right when the circumstances designated by the statutes are found to exist.[21] As partition is a matter of right incident to ownership of an undivided share, the court reached the logical conclusion that the mother could not, by making a disposition of her interest, defeat the right to partition which complainant had acquired through the will of his father.

Alex A. Alston, Jr.

[19]Kean v. Tilford, 81 Ky. 600 (1884).

[20]See Adams v. McKee, 121 Misc. 215, 200 N.Y. Supp. 765 (Sup. Ct. 1923).

[21]*E.g.*, Wolfe v. Galloway, 211 N.C. 361, 190 S.E. 213 (1937).

RECENT BOOKS

FORMS OF BUSINESS AGREEMENTS WITH TAX IDEAS, Annotated

By William J. Casey, New York: Institute for Business Planning, Inc., 1961. Pp. 718. $19.50.

Mr. Brown, residing in a medium sized city in Mississippi, owns unimproved land within the area in which the city is expanding. He is a member of a partnership engaged in the manufacture and sale of chemicals according to secret formulae; he owns sixty per cent of the stock in a corporation by which he is employed and to which he devotes most of his time, which corporation is engaged in the business of the manufacture and sale of a stable product. He desires to acquire a new home. Mr. Brown wishes to sell his interest in the partnership; desires assurance of a reasonable price for his stock in the corporation at his death; desires to construct his house with consideration being given the best tax advantage to him; desires to sell a portion of the unimproved real estate and to lease a portion of it for industrial purposes. The above situation is a greatly simplified statement of the facts which might exist from time to time with any individual in any city, no matter how large or small. To fulfill the desires of Mr. Brown a written agreement should be executed in each instance, and in each instance consideration should be given to the impact of taxes according to the method utilized to accomplish his purposes. For instance, the sale of the partnership interest may be accomplished in a number of ways. The partnership may be dissolved and the individual partners may sell to other individuals or corporations; or they may desire to sell to an existing corporation in exchange for stock, one to remain employed by the existing corporation and Mr. Brown to continue with the other corporation to which he devotes most of his time. In the sale of the partnership interest secret formulae may be involved, and Mr. Brown or his partner may desire to retain ownership with a royalty agreement. Mr. Brown's desire to secure a reasonable price for his part in the corporation in which he has controlling interest may be accomplished by a "Buy and Sell Agreement" between him and the other stockholders or a "Buy and Sell Agreement" between him and the corporation, and this may be funded by insurance. He may contract to build his house and pay the interest needed in order to finance this himself, thus acquiring an interest deduction for his taxable year, or he may elect to capitalize such interest.

The complications attendant with the development or leasing of his unimproved real estate in so far as taxation is concerned are many. He may be considered as a real estate developer. In his lease agreement he may acquire the improvements upon the termination of the lease in addition to rental paid during its term. He may secure advance rentals in a year in which he has low income rather than a succeeding year in which he has a high income. He may exchange a portion of his unimproved realty for an unimproved residence site upon which to build his new house, in which event there may be no gain or loss taxable to him at that time.

The income tax law and rates for a long time have affected the every day life of almost everyone in the nation. There is rarely a trans-

action of any size which does not have its tax consequence. All practicing lawyers are constantly confronted with situations in which tax should be of prime consideration.

Mr. William J. Casey, Editor for the Institute for Business Planning, Inc., has assembled in the book under review a myriad of agreements relating to nearly all forms of business transactions, which have been drafted with the primary view of affording the best tax consequence for the participants, and in a manner that the expected tax consequence should follow. To make a full review of this book, which is primarily a form book, would be almost like reading its table of contents, but at the risk of boredom, it should be pointed out that the volume contains agreements relative to the following.

Pre-incorporation contracts and corporate organization agreements are first. Partnerships and many of their attendant questions follow and are treated in almost complete form. For an existing corporation corporate control agreements are included, relating to management, stock purchases, redemption of stock and business insurance for purposes of protecting the corporation and for the funding of "Buy and Sell Agreements." Employment agreements for salesmen, executives, etc., based on variations as to compensation, deferred or otherwise, and stock options are treated fully.

Agreements relating to professional retainers of attorneys, architects, etc., are included along with management agreements and brokerage agreements. One section deals with the sale of goods and includes the method of pricing, installment sales contracts, quantity adjustment, discount clause, passage of title, delivery, and other questions arising in the field of the sale of goods.

Agreements for sales agencies, distributorships, advertising, manufacturing, building, servicing, and warehouse and storage are included, each being a separate heading, and each having its own special forms of agreements and clauses relating thereto.

On contracts relating to patents or similar property rights, know-how, ideas and technical services, literary and artistic property, trademarks, and trade names are present. In the field of financing, various forms of notes, debenture bonds, convertible bonds, trust agreements, indenture clauses, along with many other forms of agreements necessary to a business and its financing, are all included. One section is devoted to deposit and escrow agreements and another to guaranty and indemnity agreements.

There are sections dealing with the questions attendant in real estate transfers, such as sale and lease-back, allocation of purchase price among land and buildings, assignments of the contracts, leases of real estate, and equipment leasing.

Many practitioners will appreciate the very full treatment of the agreements relating to the sale of a business, which includes the sale of an individual proprietorship, partnership interests, or all the assets of a partnership, stock of the corporation, or the corporate assets. Also treated are the stock-for-stock acquisition and the stock for asests acquisition, which are under the heading "Plan and Agreement of Reorganization." To take care of the business in trouble a section has been devoted to compromise and settlement of claims, both before and after litigation; agreement by creditors' committees to liquidate a business or operate as a going concern; composition of creditors and other agree-

ments which would be helpful in a bankruptcy or reorganization proceeding.

What will be very helpful is the fact that under each separate heading the author lists the practical considerations and legal requirements as to the questions for which agreements are to be drawn, and following this are the tax considerations, listed in detail and in succinct, readable language. One not an expert in tax matters can read the two or three pages devoted to tax considerations and then better understand the necessity of certain clauses, considerations and recitations made in the agreements which are thereafter set forth. Further, in footnotes and in introductions to many of the agreements, the author has explained as to the particular agreement under consideration the necessity of certain provisions, citing the requirements of the Internal Revenue Code and showing how the agreement complies therewith.

No one lawyer can be an expert in the drafting of all of these forms. As a consequence, all lawyers should find this volume valuable in setting forth examples by which to go in drafting an agreement relating to his particular problem. He will find many clauses and paragraphs in each of these agreements which will be helpful to him and which might not have been thought of without the suggestion that is offered by a form book. It is similar to the value of a file of a case through which an attorney has already struggled. As the author points out, the forms of agreements in his book, and in any form book, "are merely guides to help the business man to find his obligations and the lawyer to find his client's rights and obligations. No printed form should be used unless a lawyer has approved its applicability, or adapted it to the specific situation."

It is believed that from the standpoint of taxation, it would be well for a lawyer utilizing this form book to be more familiar with questions of federal income taxation than as explained in the book. His research should go deeper than the explanations given in the book, or he should consult with one already familiar with the tax questions involved.

All in all it is believed that this book should prove a very valuable aid in any law office, regardless of tax aspects, and particularly in a law office wherein tax matters are a specialty. As the author states, "the Tax Collector has become a third party in interest in virtually every business transaction," and it is believed that this volume will go far in aiding and assisting the lawyer and his client.

Sydney A. Smith, Jr.
Wise, Smith and Carter
Jackson, Mississippi

BOOKS RECEIVED

FUNDAMENTALS OF LEGAL RESEARCH. Erwin H. Pollack. Brooklyn: The Foundation Press, Inc., 1962. Pp. 542. $8.00.

HOWELL'S COPYRIGHT LAW. Alan Latman. Washington, D.C.: BNA Incorporated, 1961. Pp. 358. $9.25.

LASSER'S ENCYCLOPEDIA OF TAX PROCEDURES. J. K. Lasser. Englewood Cliffs, New Jersey: Prentice-Hall, Inc., 1960. Pp. 1210. $29.50.

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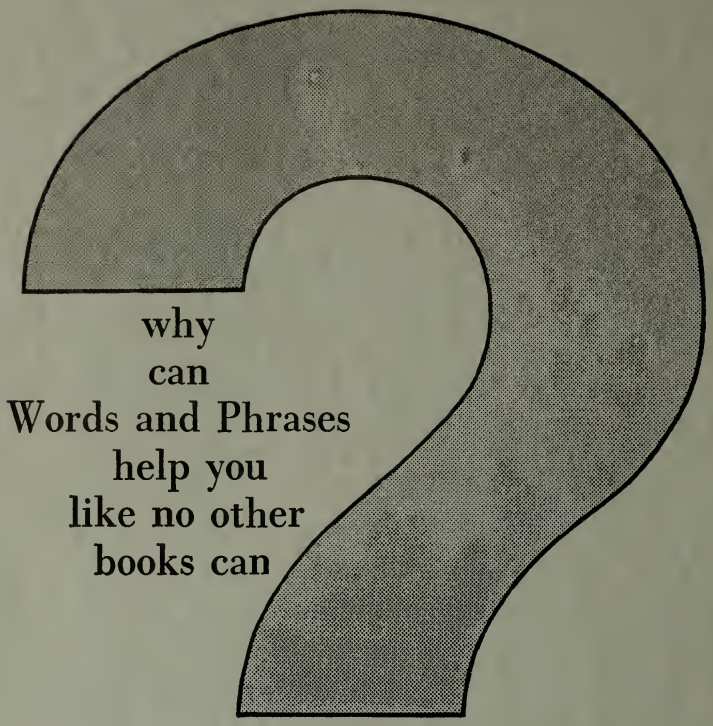

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